Draft
Analysis of Issues and Procedures for Implementation of Provisions Contained in the Line Item Veto Act (Public Law 104-130) Relating to Limited Tax Benefits

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Joint Committee on Taxation

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CONTENTS

INTRODUCTION

On April 9, 1996, President Clinton signed the Line Item Veto Act (the "Act").[1] The Act permits the President to veto certain spending provisions and limited tax benefits. The provisions of the Act take effect on January 1, 1997,[2] and sunset after December 31, 2004. Under the provisions of the Act, the Joint Committee on Taxation is required to identify provisions that constitute limited tax benefits that are subject to the President's line item veto authority.

This document[3], prepared by the staff of the Joint Committee on Taxation as a recommendation to the Members of the Joint Committee on Taxation and for the benefit of Members of Congress and their staffs and the general public, is a proposed approach outlining the principles that will be applied by the Joint Committee staff in discharging the responsibilities of the Joint Committee on Taxation under the Act. Part I of the document discusses the provisions of the Act relating to limited tax benefits. Part II describes the legislative history of the Act and discusses general principles relating to the definition of limited tax benefits. Part III analyzes in detail specific issues under the Act, and Part IV provides examples of how the Joint Committee on Taxation staff intends to interpret the provisions of the Act.

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[1] S. 4, Public Law 104-130 (April 9, 1996), which amended Title X of the Congressional Budget and Impoundment Control Act of 1974 (2 U.S.C. 681 et seq.).

[2] Technically, the provisions of the Act take effect on the earlier of (1) the day after the enactment of an act entitled "an Act to provide for a seven-year plan for deficit reduction and achieve a balanced Federal budget;" or (2) January 1, 1997. However, because the Congress has adjourned *sine die* for the 104th Congress, the provisions of the Act as a practical matter will not take effect before January 1, 1997.

[3] This document may be cited as follows: Joint Committee on Taxation, *Draft Analysis of Issues and Procedures for Implementation of Provisions Contained in the Line Item Veto Act (Public Law 104-130) Relating to Limited Tax Benefits*, (JCX-48-96), November 12, 1996.

I. DESCRIPTION OF THE LINE ITEM VETO ACT RELATING TO LIMITED TAX BENEFITS

A. Overview

The Line Item Veto Act (the "Act") amends the Congressional Budget and Impoundment Act of 1974 (the "Budget Act") to expand the President's impoundment authority with respect to spending provisions and to give the President the authority to cancel "limited tax benefits". The provisions of the Act take effect on January 1, 1997,[4] and expire after December 31, 2004. Under the Act, the Joint Committee on Taxation (the "Joint Committee") is responsible for identifying provisions that constitute limited tax benefits that are subject to the President's line item veto authority. The Act also provides for expedited procedures for Congressional review of items that have been canceled by the President pursuant to the Act.

B. Definition of Limited Tax Benefits

In general

Subject to certain exceptions, the Act defines a "limited tax benefit" as any provision that modifies the Internal Revenue Code that is either (1) a revenue-losing provision that provides a Federal tax deduction, credit, exclusion, or preference to 100 or fewer beneficiaries in any fiscal year for which the provision is in effect; or (2) a Federal tax provision that provides temporary or permanent transitional relief to 10 or fewer beneficiaries in any fiscal year.

Revenue-losing provisions

A provision is defined as "revenue-losing" if it results in a reduction in Federal tax revenues either for the first fiscal year for which the provision is effective or for the five-year period beginning with the first fiscal year for which the provision is effective. However, the Act provides that a revenue-losing provision that affects 100 or fewer beneficiaries in a fiscal year is not a limited tax benefit if any of the following exceptions are satisfied. First, if a provision has the effect of providing all persons in the same industry or engaged in the same activity with the same treatment, then the provision is not a limited tax benefit even if 100 or fewer persons benefit. A second exception is for provisions that have the effect of providing the same treatment to all persons owning the same type of property or issuing the same type of investment instrument. Finally, a provision is not a limited tax benefit if the only reason the provision affects different persons differently is because of: (1) the size or form of the business or

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[4] The provisions of the Act technically take effect on the earlier of (1) the day after the enactment of a law entitled "An Act to provide for a seven-year plan for deficit reduction and achieve a balanced Federal budget;" or (2) January 1, 1997. However, because the 104th Congress has adjourned *sine die*, the provisions of the Act will not, as a practical matter, take effect before January 1, 1997.

association involved; (2) general demographic conditions affecting individuals, such as their income level, marital status, number of dependents, or tax return filing status; (3) the amount involved; or (4) a generally-available election provided under the Internal Revenue Code.

Provisions providing transitional relief

A Federal tax provision that provides temporary or permanent transitional relief to 10 or fewer beneficiaries in any fiscal year is a limited tax benefit (even if the provision does not lose revenue relative to present law) unless the provision (1) provides for the retention of prior law for all binding contracts or other legally enforceable obligations in existence on a date contemporaneous with Congressional action specifying such a date, or (2) is a technical correction to previously enacted law (that is estimated as having no revenue effect).

Special rules for determining the number of beneficiaries

In determining the number of beneficiaries affected by a provision, the Act requires certain individuals and businesses to be aggregated: all businesses and associations which are related (within the meaning of Internal Revenue Code sections 707(b) and 1563(a)) are treated as one beneficiary; all qualified plans of a single employer are treated as one beneficiary; and all holders of the same bond issue are treated as one beneficiary. In addition, if a benefit is provided to a corporation, partnership, association, trust, or estate, the Act provides that the individual shareholders of the corporation, partners of the partnership, members of the association, or beneficiaries of the trust or estate should not also be counted as beneficiaries of the provision.

C. Procedural Requirements

Identification of limited tax benefits

Under the Act, the Joint Committee is required to examine any revenue or reconciliation bill or joint resolution that amends the Internal Revenue Code prior to its filing by a conference committee in order to determine whether or not the bill or joint resolution contains any limited tax benefits. Upon review of the bill or joint resolution, the Joint Committee is required to issue a statement that either (1) identifies each limited tax benefit included in the bill or resolution, or (2) states that the bill or resolution contains no limited tax benefits. The Joint Committee statement must be submitted to the conference committee on the bill or joint resolution and made available by the Joint Committee to any Member of Congress upon request. The decision of whether to include the Joint Committee's identification of limited tax benefits in a bill or joint resolution that amends the Internal Revenue Code is left to the discretion of the conferees on the bill. However, if the conferees choose to include the Joint Committee information, all limited tax benefits identified by the Joint Committee must be included--the conferees may not selectively include some of the limited tax benefits and exclude others. The congressional identification of a limited tax benefit in a conference report is not subject to judicial review.

If the conference report includes the information from the Joint Committee identifying provisions in the conference report that are limited tax benefits, then the President may cancel one or more of those, but only those, provisions that have been identified. If such a conference report contains a statement from the Joint Committee stating that none of the provisions in the conference report are limited tax benefits, then the President has no authority to cancel any of the tax provisions, because there are no tax provisions that are eligible for cancellation under the Act. Finally, if legislation amending the Internal Revenue Code does not contain the information provided by Joint Committee (either because there is no conference report or because the conference report does not include such information), then identification of any limited tax benefit in such legislation may be made by the President (within the confines of the definition set forth in the Act). If any provision qualifies as a limited tax benefit, and the President identifies the provision as such, the President may exercise his cancellation authority with respect to that provision.

If the conferees decide to include in the conference report the Joint Committee's identification of limited tax benefits, the Act specifies the exact format for including such information. At the end of the bill, a separate section would read as follows: "Section 1021(a) of the Congressional Budget and Impoundment Control Act of 1974 shall _____ apply to _____", with the blank spaces being filled in with the appropriate information. If the Joint Committee has identified limited tax benefits in a conference report, the word "only" would appear in the first blank and a list of all of the provisions of the bill or joint resolution identified in the Joint Committee statement would appear in the second blank. If the Joint Committee has determined that there are no limited tax benefits in the conference report, the word "not" would appear in the first blank and the phrase "any provision of this Act" would appear in the second blank. Again, the conferees may not pick and choose between the limited tax benefits identified by the Joint Committee---if the Joint Committee has identified limited tax benefits in a bill, the conferees either must list all of the provisions that have been so identified, or must omit the Joint Committee information in its entirety.

Procedures following exercise of Presidential authority

If the President cancels any tax or spending provisions within a law, a special message must be transmitted to Congress within five calendar days (excluding Sundays) of enactment of the law to which the cancellations apply. The special message must be transmitted to both Houses of Congress on the same day. If the House is not in session, the special message must be delivered to the Clerk of the House of Representatives, and if the Senate is not in session, to the Secretary of the Senate. One special message would be submitted with respect to each law within which a cancellation is made. The President's special message must include detailed information about the items canceled and the reasons therefor, including the dollar amount of the items which have been canceled, the estimated fiscal, economic and budgetary effect of each cancellation, and, if applicable, the specific States and Congressional districts impacted by the cancellation. For each limited tax benefit canceled from a law, the Office of Management and Budget is required to estimate the deficit decrease caused by the cancellation as a separate entry in its pay-as-you-go report to Congress. However, the Act provides that the savings from such

cancellations shall not be included in the pay-as-you-go balances under the Balanced Budget and Emergency Deficit Control Act, in order to ensure that the savings are devoted to deficit reduction and are not available to offset a deficit increase in another law. The Act also requires that the Congressional Budget Office submit an estimate of the savings resulting from a cancellation to the Budget Committees of the House and Senate.

Cancellation of a limited tax benefit means that the specific provision that provides the benefit has no legal force or effect (i.e., it is as if the provision never had been enacted). The cancellation becomes effective when the President's message is received in both the House of Representatives and the Senate. The cancellation of any provision is nullified only if a disapproval bill is enacted into law. If a cancellation is disapproved in a disapproval bill (i.e., if the Congress votes to reinstate the provision), the provision's effective date will be the original date provided in the law to which the cancellation applied.

Expedited procedures are provided for consideration of a disapproval bill introduced in either House within five calendar days of session (i.e., days in which both Houses of Congress are in session) following receipt of the President's special message. Congress is provided 30 calendar days of session to consider a disapproval bill under these expedited procedures. If Congress adjourns at the end of a Congress prior to the expiration of the 30-day period, and a disapproval bill was then pending in either House of Congress or before the President, a new disapproval bill for the same special message may be introduced within the first five calendar days of session of the new Congress, and the new Congress would be provided 30 calendar days of session to consider the new disapproval bill under the expedited procedures. Only one bill may ultimately be acted upon for each special message using these expedited procedures.

In order for a disapproval bill to qualify for the expedited procedures in the House of Representatives, the introduced bill must disapprove all of the cancellations in the special message to which the disapproval bill relates. The disapproval bill would be referred to the appropriate committee or committees, who must report it without amendment, and with or without recommendation, within seven calendar days of session after the date of its introduction. The bill would be considered on the House floor under expedited procedures. No amendment would be in order, except that if fifty Members agree, an amendment may be offered on the House floor to strike one or more canceled items from the disapproval bill.

Any member of the Senate may introduce a disapproval bill containing any combination of cancellations included in the President's special message. The disapproval bill would be referred to the appropriate committee or committees, who must report it with or without amendment no later than seven calendar days of session after the date of its introduction. The bill would be considered on the Senate floor under expedited procedures. Amendments to a disapproval bill would be strictly limited to those amendments that either strike or add a cancellation that is included in the President's special message.

In the case of disagreement between the two Houses of Congress with respect to a disapproval bill passed by both Houses, conferees must be promptly appointed and a conference

promptly convened. The conferees on a disapproval bill must include in the conference agreement any cancellations upon which the two Houses have agreed, and may include any or all cancellations upon which the two Houses have disagreed, but they may not include any cancellations that were not included in either House's version of the disapproval bill. Expedited procedures are provided in both Houses for consideration of a conference agreement on a disapproval bill.

II. LEGISLATIVE HISTORY AND DISCUSSION OF PRINCIPLES DEFINING LIMITED TAX BENEFITS

A. History of the Line Item Veto

1. In general

President Grant first proposed a Presidential line item veto in 1876 in response to the Congress' growing practice of attaching riders to appropriations bills. In 1938, the House of Representatives approved a line item veto amendment by voice vote, but the Senate did not accept it.

The modern push for the enactment of a line item veto can be traced to the Budget Act. The concept of impoundment relates to any action by the President to withhold or delay the spending of appropriated funds. Prior to 1974, the President had limited authority not to spend appropriated funds. In the 1950s and 1960s, disputes over this impoundment authority grew as Presidents refused to fund certain weapons systems to the extent authorized by the Congress.[5]

These disputes over the impoundment authority of the President led to enactment of the Budget Act. Under the Budget Act, the President is permitted to delay the expenditure of appropriated funds and to cancel funds (rescission authority). In the case of a rescission, the Budget Act requires that the Congress affirmatively approve the rescission action within 45 days or the appropriated funds must be spent.

In his State of the Union address in 1984, President Reagan called for a constitutional amendment providing the President with line item veto authority. Since that time, there have been various legislative attempts to pass a line item veto measure. This effort culminated in the enactment of the Line Item Veto Act (the "Act") on April 9, 1996.

The Act enhances the President's authority under the Budget Act and, in certain cases, shifts the burden so that the Congress must disapprove the President's cancellation of certain spending and limited tax benefit provisions. In addition, the Act expands the Budget Act to tax provisions for the first time. The Joint Explanatory Statement of the Committee of Conference (the "Statement of Managers") for the Act states that "if Presidents had applied this authority [the line item veto authority] to all matters objected to in Statements of Administration Policy on spending bills in the fiscal years 1984 through 1989, spending could have been reduced by a six-year total of about $70 billion."

A total of 43 States have enacted line item veto legislation. These State laws differ from the provisions of the Act in two important respects. First, under the procedures that apply in each of

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[5] Virginia A. McMurtry, CRS Issue Brief, "Item Veto and Expanded Impoundment Proposals," Order Code IB89148 (Updated September 20, 1996).

the 43 States with the line item veto, the Governor is permitted to exercise his or her veto authority over the provisions of a bill before it becomes law. In theory, this differs from the procedure that applies under the Act, where the President must approve the underlying legislation before his or her authority to veto designated items is effective. Further, none of the States having a line item veto extend that veto authority to tax provisions. In contrast, the Act permits the President to veto certain limited tax benefits that have been identified by the Congress.

2. House bill (H.R. 2)

Under the version of the Act approved by the House of Representatives (H.R. 2), the President was provided "enhanced rescission" authority to veto any targeted tax benefit if the President determined that the veto would (1) help reduce the Federal budget deficit, (2) not impair any essential government functions, and (3) not harm the national interest.

The House version of the Line Item Veto Act originally was reported by the House Committee on Rules on January 27, 1995,[6] and by the Committee on Government Reform and Oversight on January 30, 1995.[7]

Under the original House Committee on Rules version of H.R. 2, a targeted tax benefit was defined as any provision of a revenue act that the President determines would provide a Federal tax benefit to 5 or fewer taxpayers. The version of H.R. 2 reported by the Committee on Government Reform and Oversight defined a targeted tax benefit to mean any provision of a revenue or reconciliation Act that the President determines would provide a Federal tax benefit to 100 or fewer taxpayers. Under this version of the bill, any partnership, limited partnership, trust or S corporation, and any subsidiary or affiliate of the same parent corporation would be counted as a single beneficiary.

On February 1, 1995, the House Committee on Rules reported a rule for House floor consideration of H.R. 2.[8] Under the rule, an amendment in the nature of a substitute was made in order. Under this amendment in the nature of a substitute, a targeted tax benefit was defined to mean "any provision of a revenue or reconciliation act determined by the President to provide a Federal tax deduction, credit, exclusion, preference, or other concession to 100 or fewer beneficiaries." Any partnership, limited partnership, trust, or S corporation, and any subsidiary or affiliate of the same parent corporation, was treated as a single beneficiary regardless of the number of partners, limited partners, beneficiaries, shareholders, or affiliated corporate entities.

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[6] House Report 104-11, Part 1 (January 27, 1995).

[7] House Report 104-11, Part 2 (January 30, 1995).

[8] House Report 104-15 (February 1, 1995).

There was considerable debate on the House floor about the 100 or fewer beneficiaries threshold. A number of amendments were offered to adopt a test that would not apply a numerical threshold test to determine whether a provision was subject to the line item veto. During this debate, a number of Members argued that a numerical threshold would limit the scope of the line item veto provision in an unacceptable manner. However, Congressman Peter Blute (R-MA) stated that the numerical threshold was a carefully crafted compromise designed to accommodate the concerns of all Members.[9] He further stated:

> "Following discussions in committee where Members concluded that the language . . .which limited the category to five or fewer taxpayers was too restrictive, we accepted a bipartisan amendment to change the definition to include 100 or fewer taxpayers, again seeking to get at rifle shots or special deals.
>
> "I can tell you the Committee on Ways and Means people are not happy, believing that we have once again broadened the category well beyond fixing the problem. Nevertheless, we support the language reported by our committee and included in the base text as sufficiently broad to fix the problem of special deals, while narrow enough to prevent the President from vetoing such general purpose provisions as the middle class tax cut or child care tax credit."

In response to Congressman Blute's comments, Congresswoman Carolyn Maloney (D- NY) countered:

> ". . .the fundamental problem remains. The artificial numerical number can easily be fudged. Any smart lawyer will easily write tax loopholes to avoid the President's veto. It will simply benefit 101 or 102 people. Then the President will not be able to strike it down."[10]

Congressman John Spratt (D-SC) spoke at length about the fact that the House bill language would not cover the type of tax benefits that Members might expect to be subject to the line item veto. In his remarks, he discussed the analogy between spending provisions and special interest tax provisions and pointed out that the Congress often used tax benefits to provide incentives or subsidies (such as a tax credit for people who install solar heat in their homes) that would not otherwise be provided through the appropriations process. He argued that such provisions should be subject to the line item veto and offered an amendment to adopt language that would not apply a numerical threshold to determining whether a tax provision was subject to the line item veto. This amendment was defeated by a vote of 175-243. Also defeated (by a vote of 196-203) was an amendment by Congresswoman Louise Slaughter (D-NY) to expand the definition of targeted tax benefit to include any provision that has the practical effect of providing a benefit in the form of different treatment for a particular taxpayer or a limited class of taxpayers. Finally, the House defeated (by a vote of 185-241) a motion by Congresswoman Cardiss Collins

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[9] Congressional Record, February 2, 1995, H1120.

[10] *Ibid.*

(D-IL) to recommit the bill with instructions to the Committee on Government Reform and Oversight to define a targeted tax benefit as any provision that has the practical effect of providing a benefit in the form of different treatment to a particular taxpayer or a limited class of taxpayers, whether or not such provision is limited by its terms to a particular taxpayer or class of taxpayers, but that does not include any benefit provided to a class of taxpayers distinguished on the basis of general demographic conditions such as income, number of dependents, or marital status.

3. Senate bill (S. 4)

The original Senate version (S.4) of the Act reported by the Committee on the Budget and the Committee on Governmental Affairs did not apply the President's line item veto authority to tax provisions.[11] However, the final Senate bill gave the President line item veto authority by requiring each item of spending in an appropriation bill and each item of new direct spending or any targeted tax benefit in any authorizing bill to be enrolled as a separate bill.[12] Thus, under the Senate bill, the President would have been permitted to exercise his veto power over any number of these separately enrolled bills. Under the Senate bill, a targeted tax benefit included any provision that (1) was estimated to lose revenue in the first fiscal year, the first five fiscal years, or the second five fiscal years covered by the budget resolution and (2) had the practical effect of providing more favorable treatment to a taxpayer or a targeted group of taxpayers when compared to a similarly situated taxpayer or group of taxpayers. Unlike the House bill, the Senate bill provision applied regardless of the number of taxpayers who might benefit from a provision.

There was extensive debate on the Senate floor concerning the effect of the language in the Senate bill relating to the definition of a targeted tax benefit in comparison to the language in the House bill. For example, Senator John McCain (R-AZ) stated that the intent of the Senate bill language was to apply the line item veto to the so-called transition rules in which "tax breaks are included for favored individuals or companies. . .The bill is intentionally narrowly focused on targeted tax benefits to prevent the same kind of abuses that have become rampant in the appropriations process."[13]

Senator Dan Coats (R-IN) also discussed the analogy to provisions in spending bills. He said that the Senate bill ". . .would not allow the President to veto a broad tax deduction on the books, or a broad tax provision such as mortgage interest deductions. . .But it would go to those

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[11] See Senate Report 104-9 (Budget Committee, February 27, 1995) and Senate Report 104-13 (Governmental Affairs, March 7, 1995).

[12] Senator Bob Dole (R-KS) offered an amendment on the Senate floor, which was adopted and became the substance of the Senate's line item veto legislation.

[13] Congressional Record, March 21, 1995, S4213.

specifically targeted items that often are added somewhere along the line in the tax-writing process and go, not to benefit a target group, but go to benefit a very specific targeted interest."[14]

Further, in support of the Senate bill language, Senator Larry Craig (R-ID) stated "[the line item veto]. . .should apply only in cases where similarly situated taxpayers within a group are targeted directly and are arbitrarily dealt with in tax legislation."[15]

On the other hand, some Senators argued that the Senate bill was unacceptably narrow because it looked only at whether a targeted group of taxpayers was treated more favorably than a similarly situated group of taxpayers. In remarks made on the Senate floor on March 22, 1995, Senator Bill Bradley (D-NJ) stated:

> ". . .the language of the Dole substitute is even more unclear on tax expenditures than the 100 taxpayer language used in the [House bill]. . .What does this definition mean? What does a similarly situated taxpayer mean in this context? . . .Under this definition, could Congress give special tax breaks to a specific industry such as the oil and gas industry, and shield these tax giveaways from the President's line item veto because all companies within the favored industry would be allowed to claim the same special interest tax break?"[16]

In later remarks, Senator Bradley said:

> "The debate on this floor evidences the clear intent of the supporters of this bill to subject tax loopholes to a Presidential veto, and therefore it includes the tax loophole for the Members of Congress, it includes the tax loophole for the Virgin Islands corporations, and it includes other new and expanded tax loopholes."[17]

In an attempt to respond to criticism of the Senate bill language relating to targeted tax benefits, Senators Bob Dole (R-KS), Pete Domenici (R-NM), and Bob Packwood (R-OR) sent a letter dated March 22, 1995, to Senators Tom Daschle (D-SD), James Exon (D-NE), and John Glenn (D-OH) to respond to questions raised about the Senate bill language.[18] In this letter, Senators Dole, Domenici, and Packwood made the following points:

> "We are concerned, however, that implicit in your questions is a fundamental misunderstanding of the objectives of the substitute. The treatment of targeted tax benefits

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[14] Congressional Record, March 21, 1995, S4221.

[15] Congressional Record, March 21, 1995, S4223.

[16] Congressional Record, March 22, 1995, S4304.

[17] Congressional Record, March 22, 1995, S4307.

[18] See Appendix B for a copy of this letter.

mirrors the treatment of special interest, spending provisions in authorization or appropriation bills. Fairness dictates that if rifleshot spending provisions are subject to the veto pen, then rifleshot tax provisions benefitting a single taxpayer or a handful of taxpayers should also be subject to the veto pen. It may be too simple to suggest that we all know them when we see them -- but common sense should be an obvious test in these matters.

"The concept of 'similarly situated taxpayers' is an important one. A provision that only affects a few taxpayers is not in and of itself a targeted tax benefit. Because of the complex nature of our economy, there are many instances in which there are only a relatively small number of taxpayers engaged in a particular activity. If all taxpayers engaged in a particular activity are treated the same, then there is no targeted tax benefit; however, if some of those taxpayers are given more favorable tax treatment, there would be a targeted tax benefit.

"For example, the current tax code has a provision that eases the estimated tax requirements on farmers based on the fact that the income of farmers is particularly difficult to estimate. Farmers' earnings are at the mercy of a host of natural events, such as weather, insects and disease. If the estimated tax rule were enacted after the line item veto measure, it would not be a targeted tax benefit because all similarly situated taxpayers (i.e., farmers) are treated the same.

"The determination of whether or not a provision is a targeted tax benefit is based on the substance of the provision, not just the form in which it is drafted. That's why the pending bill applies the targeted tax benefit concept to a provision having the practical effect of providing more favorable tax treatment.

"The targeted tax benefit concept is intended to be a narrower concept than the tax expenditure concept. A targeted tax benefit gives favorable tax treatment to a single taxpayer or a limited group of taxpayers.

"The targeted tax benefit concept does not apply to changes in the basic structure of the tax code. For example, an across-the-board tax cut on wage and salary income of all individuals would not be a targeted tax benefit."

B. Congressional Intent in Enacting the Line Item Veto Act

The Statement of Managers for the Act makes clear that the Congress intended to confer upon the President limited authority to cancel new spending and limited tax benefits. The Statement of Managers provides that "the purpose of the conference report is to promote savings by placing the onus on Congress to overturn the President's cancellation of spending and limited tax benefits." While the Congress clearly did not intend to give the President unfettered authority to cancel tax benefits, it also is clear that the Congress did intend the veto authority to apply in certain limited tax cases.

It is evident that the Congress was concerned about the possible scope of the new line item veto authority. Thus, the Statement of Managers states:

> "The conferees note that while the conference report delegates new powers to the President, these powers are narrowly defined and provided within specific limits. The conference report includes specific definitions, carefully delineates the President's cancellation authority, and provides specific limits on this cancellation authority. The delegation of this cancellation authority is not separable from the President's duties to comply with these restrictions. . . Given the significance of this delegation, the conference report includes a sunset of this authority."[19]

With respect to the authority to veto limited tax benefits, the Statement of Managers provides the following guidance:

> "Finally, with respect to limited tax benefits, the term cancel means to prevent the specific provision of law that provides the benefit from having legal force or effect. Again, the authority granted the President is very narrow -- only to collect the tax that would otherwise not be collected or to deny the credit that would otherwise be provided. The President may not change, alter, or modify any other aspect of the law."[20]

Although the Statement of Managers does not contain any specific statements as to the intended scope of the definition of limited tax benefits relative to either the House or Senate bills, it is clear that the language in the conference agreement is both broader and narrower than the targeted tax benefit language in both the House and Senate bills. For example, the conference agreement specifically incorporates language that includes transitional rules within the definition of a limited tax benefit. Although it is clear from the history of the line item veto that these transitional rules were precisely the type of provision to which the legislation was intended to apply, neither the House nor the Senate bill specifically applied to these provisions. Of course, the original House bill likely would have applied to most transition rules because the number of beneficiaries would be below the numerical threshold contained in the bill. However, because the Senate bill applied only to revenue-losing provisions, there was some question as to whether so-called transition rules, which often merely maintain present-law tax treatment for certain taxpayers, could be considered as subject to the line item veto.

At the same time, by incorporating language from both the House and the Senate bills, the conference agreement also is likely to apply to fewer provisions than under either of those bills. For example, the conference agreement generally incorporates the standard contained in the House bill (i.e., a provision that provides a tax deduction, credit, exclusion, preference, or concession to 100 or fewer beneficiaries). However, the conference agreement includes a

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[19] House Report 104-491 (March 21, 1996), p. 19.

[20] House Report 104-491 (March 21, 1996), p. 29.

limitation contained in the Senate bill (i.e., that the provision, if not a transition rule, must be a revenue-losing provision). In addition, the Statement of Managers suggests that the exceptions (for taxpayers in the same industry, engaged in the same activity, or owning the same type of property) are intended to articulate the exception in the Senate bill that the line item veto does not apply if the effect of the provision is that similarly situated taxpayers are treated the same. Thus, it is clear that the conferees intended to limit the provisions that would be subject to the line item veto. This intent would appear to be consistent with the conferees' statement that the legislation was intended to provide limited and temporary authority to the President to cancel new spending and limited tax benefits.

The House and Senate floor debate on the conference agreement to the Act indicates that the Members of Congress recognized the relatively limited scope of the conference agreement language relating to limited tax benefits.

For example, Congresswoman Slaughter suggested that the limited tax benefit provision had been narrowed in the conference agreement "to the point of nonrecognition. . .when it comes to tax benefits and tax policy, given to favorite constituents or constituent groups, nobody is going to be touching that."[21] In addition, Congressman David Skaggs (D-CO) argued that a "tax break for a particular industry that takes millions of dollars out of the Federal treasury can't be canceled by the President."[22]

In response to these types of concerns, Congressman Jim Bunning (R-KY) stated:

"To those who wanted us to include more on taxes, I would simply remind them that our financial problems have not been caused by too few revenues but by too much spending.

". . .The limited tax provisions which appear from time to time in a large tax bill. . .are now going to be subject to the line item veto.

". . .I feel confident that the President will see the good policy behind some of these very narrow tax breaks such as the orphan drug tax credit which provides a tax incentive for research into drugs for rare diseases.

". . .I would also remind those who think that we should have gone farther on allowing the President to item veto tax provisions to remember that tax breaks allow people to keep their own money."[23]

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[21] Congressional Record, March 28, 1996, H3002.

[22] Congressional Record, March 28, 1996, H3014.

[23] Congressional Record, March 28, 1996, H2979.

There was even more discussion about the scope of the conference agreement on the Senate floor. Senator John McCain said ". . .this is not the approach I would have preferred. I believe that the Senate language developed with Mr. Bradley would have been more effective. However, as we all know, compromise often must occur in conference. The results can be seen here."[24]

Further, Senator Ted Stevens (R-AK) pointed out that the conference agreement was a compromise, but expressed concern about its scope. He stated the following:

> "In the area of taxes, the conference report does not go as far as I would have liked. But it was the best that we could get the conferees to agree to.
>
> ". . .It may well be that, although we are starting toward an attempt to give the President the right to eliminate limited tax breaks, we may have so defined limited tax breaks that they will never be touchable by the veto pen."[25]

Senator Robert Byrd (D-WV) spoke at length about the scope of the conference agreement. In his remarks, Senator Byrd stated:

> "By limiting the President's rescission authority to only those tax expenditures that, by definition, benefit 100 or fewer taxpayers, S. 4 absurdly restricts the ability of the President to get at this type of backdoor spending.
>
> "How absurd is this? Imagine limiting the scope of the President's rescission authority to those appropriations that impacted 100 or fewer beneficiaries. Imagine the wrath of verbal indignation that would befall any Senator who stood up here and proposed that kind of rescission process.
>
> ". . .Mr. President, the concept of numerical definitions on tax expenditures was rejected in the Senate because we all know that any tax lawyer worth his salt can find a few extra people to qualify for the targeted tax benefit, thereby bringing the number of beneficiaries above 100 and out of range of rescission authority. Consequently, this limitation is nothing more than an open invitation to the many creative tax attorneys in this country to find ways to abuse the system.
>
> "But the asininity of such a provision does not stop there. The definition of a tax expenditure, or 'limited tax benefit' as S. 4 calls it, is further gutted with exemptions for tax breaks that serve to benefit all persons in the same industry, or all persons engaged in the same type of activity, or even all persons owning the same type of property. Thus, under that

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[24] Congressional Record, March 27, 1996, S2931.

[25] Congressional Record, March 27, 1996, S2956.

definition, a special tax break passed by the Congress for anyone owning a Rolls Royce, for example, would not be subject to a presidential rescission since everyone affected would own the same type of property, in this case a Rolls Royce."[26]

A number of other Democratic Senators made points similar to Senator Byrd. In addition, Senator Daniel Patrick Moynihan (D-NY) made the following point:

"The tax-writing committees often and properly find that tax relief may be justified in narrow circumstances. Such narrow relief is and ought to be granted sparingly, yet these features of the bill [the numerical thresholds and the exceptions that apply to them] create a perverse incentive to craft broader tax benefits than necessary in order to avoid application of the line item veto. This is surely counterproductive."[27]

On the other hand, Senator Bill Roth (R-DE) expressed concern about the fact that the conference agreement applied to limited tax benefits at all. He argued that the notion of subjecting a tax cut to the line item veto was unprecedented and pointed out that none of the 43 States with the line item veto applied it to tax provisions. However, he stated that "Fortunately, the President's authority in the tax area is narrow -- evidence of the fact that the conferees understood the anomaly of impounding tax cuts."[28]

C. General Principles for Joint Committee Review of Bills for Limited Tax Benefits

1. In general

Although the Act confers a specific responsibility on the Joint Committee on Taxation to identify limited tax benefits, inevitably there will be questions that arise concerning how the language of the Act should be interpreted in particular cases. The determination of whether a provision is a limited tax benefit is an inherently difficult determination, particularly because the Act requires an analysis of whether the same tax treatment is provided to all taxpayers in the same industry, engaged in the same activity, owning the same property, or issuing the same type of investment. In addition, the Act requires a different analysis for revenue-losing provisions than for transitional relief and does not address certain types of changes in the law that may raise revenue but may treat different class of taxpayers differently. This document represents the approach the staff of the Joint Committee on Taxation ("Joint Committee staff") intends to propose to the Members of the Joint Committee with respect to the implementation of the provisions of the Act relating to limited tax benefits.

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[26] Congressional Record, March 21, 1996, S2961. But see the discussion of the Joint Committee staff analysis in Part III.C.2.d., below.

[27] Congressional Record, March 27, 1996, S2973.

[28] Congressional Record, March 27, 1996, S2968.

The Act does not contain easily applied tests for determining whether a provision is a limited tax benefit. For example, if the Act merely applied to provisions that benefited 100 or fewer beneficiaries, the Joint Committee's responsibilities under the Act would be to define what constitutes a provision, to define what is a beneficiary, and to determine whether or not a particular provision benefited more than the threshold number of beneficiaries. The Act does not provide for such a mechanical approach. Because the Act requires an analysis beyond whether a provision is a revenue-losing provision or benefits fewer than the threshold number of beneficiaries, the Joint Committee staff intends to develop general principles so that the Act may be applied consistently, while considering the specific facts and circumstances underlying each provision in order to identify those provisions that it appears the Congress intended to be included as limited tax benefits in enacting the Act.

The responsibilities of the Joint Committee on Taxation relating to the Act are limited to applying a statutorily prescribed set of rules to determine whether a revenue provision is a limited tax benefit. The Joint Committee is not charged under the Act with evaluating the policy reasons underlying any particular provision. Thus, the mere fact that a provision is identified as a limited tax benefit does not constitute a judgment that the provision is bad from a policy perspective.

Further, the policy arguments either supporting or opposing the adoption of a provision are irrelevant to the determination of whether a provision is a limited tax benefit under the definition set forth in the Act. Thus, the Joint Committee staff believes that the determination of whether a provision is a limited tax benefit does not involve any judgment regarding the underlying tax and nontax policy reasons for enacting the provision. In fulfilling its responsibilities under the Act, the Joint Committee staff generally will not comment on the policy considerations.

The Joint Committee staff expects that the President and the Congress will consider each identified limited tax benefit individually and make a determination as to whether there is a sufficient policy rationale for enacting the provision despite its limited applicability.

2. Procedural issues

Under the Act, the identification of limited tax benefits is made in the conference report for any legislation that amends the Internal Revenue Code of 1986. Thus, the discharge of the Joint Committee's responsibilities under the Act will be performed as a routine part of the preparation of the conference report and Statement of Managers.

The Joint Committee staff anticipates that Members of Congress also will be concerned during the course of Congressional consideration of tax legislation about whether specific legislative proposals may be limited tax benefits under the Act. Therefore, if requested by a Member, the Joint Committee staff will provide a preliminary opinion as to whether a specific legislative proposal will constitute a limited tax benefit. Because the precise manner in which a proposal is drafted may be determinative of whether or not it constitutes a limited tax benefit, the

Joint Committee staff will not be able to provide such an opinion to Members unless a proposal is accompanied by proposed statutory language.

3. Interpreting the provisions of the Act relating to limited tax benefits

In general

The legislative history relating to limited tax benefits indicates, in the view of the Joint Committee staff, that the Congress intended the line item veto legislation to have a fairly narrow scope that ensures that the President will not be permitted to veto provisions that have the effect of treating similarly situated taxpayers in a consistent manner. The specifically enumerated exceptions that apply under the statutory language are evidence of the intent of Congress to limit the scope of the term "limited tax benefit." In addition, the fact that the line item veto authority sunsets is further indication of the concern of the Congress about the potential scope of the Act. Finally, because the line item veto statutes that apply in 43 States do not apply to tax legislation, there is no experience at the State level that is relevant for this purpose and the Act can be viewed as an experiment to see how the line item veto might be applied to tax provisions.

However, it is clear also from the legislative history that the Congress did intend certain limited tax benefits to be subject to the line item veto. For example, it is clear that certain so-called "rifle shots" (the permanent or temporary transitional rules that permit certain identified taxpayers to avoid the effects of a change in the law) are intended to be subject to the line item veto. In addition, it is clear that certain revenue-losing provisions that have 100 or fewer beneficiaries are intended to be subject to the line item veto unless a specific exception applies.

There are a number of general principles that the Joint Committee staff intends to apply in evaluating whether provisions contained in pending tax legislation are subject to the line item veto.

Definition of limited tax benefits should be analogous to special interest spending provisions

The floor debate in both the House and the Senate suggests that the Members of Congress viewed the application of the line item veto legislation to tax provisions as, in part, a way of identifying tax provisions that were the equivalent of "special interest" spending provisions. The Members expressed concern that the effects of the line item veto would be vitiated if the Act also did not apply to tax legislation because Members might be able to accomplish through tax benefits what they could not achieve directly through spending provisions.

In the case of revenue legislation, identifying the special interest provision that is subject to the line item veto likely will be difficult. Tax legislation often can be drafted in different ways that reach the same substantive result. As further discussed in Part III.A., below, in order to apply a rule similar to the rules provided for special interest spending provisions, a tax provision will not be subject to the line item veto unless (1) there is statutory language relating to the

provision that can be stricken and (2) striking such language will not otherwise alter the substance of the remaining provisions. Thus, for example, if a provision appears to affect either 100 or fewer beneficiaries (in the case of a revenue-losing provision) or 10 or fewer beneficiaries (in the case of transitional relief); but striking the relevant statutory language would affect more than the requisite number of beneficiaries, then the statutory language cannot be stricken without having a broader impact than merely affecting the beneficiaries of the limited tax benefit. In such a case, the provision would not be considered a limited tax benefit.

Substance over form

The Joint Committee staff will evaluate provisions under the Act in a manner that generally looks at the substance of a provision over its form unless to do so would be inconsistent with either the statute or prior interpretations of the Joint Committee staff. In determining whether a provision has more than the requisite number of beneficiaries, the Joint Committee staff will look at the statutory incidence of the tax benefit being conferred because to do otherwise might lead to inconsistent and arbitrary results. On the other hand, the Joint Committee staff will consider the substance of specific legislative language in identifying the "provision" that is subject to the line item veto, rather than applying a standard that looks merely at whether statutory language is within the same section, subsection, paragraph, or clause of a bill.

In addition, the Joint Committee staff will consider its estimate of the actual, rather than the intended, impact of a provision in determining the effect of the provision for line item veto purposes. For example, if a provision was drafted with the intent of having broad applicability, but a limited number of taxpayers in fact are affected and the provision otherwise constitutes a limited tax benefit, the Joint Committee staff will look at the estimated number of taxpayers who actually will benefit from the provision rather than the intended number of beneficiaries.

Although the Joint Committee staff will consider the substance of a provision rather than its form, it is clear that in certain circumstances, the manner in which a provision is drafted will determine whether or not it is a limited tax benefit. For example, if the Congress were imposing a new tax on an activity in which 60 taxpayers were engaged, but wanted to provide transitional relief to five of those taxpayers, it may be possible in some circumstances to define a class comprised of only the 55 taxpayers that would be liable for the new tax (without reference to those taxpayers being excluded from the tax). In such a case, there would be no specific statutory language that could be stricken even though the substantive effect of the provision may be the same as if the specific permanent transitional relief were separately drafted.

Revenue table not determinative

During the course of Congressional consideration of legislation, the staff of the Joint Committee typically prepares and releases a number of revenue tables showing the estimated revenue effects of legislative proposals. These revenue tables are prepared to inform the Congress as to the estimated budgetary consequences of proposals being considered and, unless specifically prepared for purposes of the Act, will not necessarily contain sufficient information

to determine whether an item is or is not a limited tax benefit. For example, a single item on a revenue table that is estimated to increase fiscal year budget receipts may, in fact, consist of several different provisions, some of which might constitute a limited tax benefit under the Act. Thus, the manner in which items are presented on a revenue table will not be determinative of whether an item is a limited tax benefit, unless the table was specifically prepared for purposes of the Act.

Limits on definition of revenue-losing provisions

The line item veto applies in the context of the current Federal tax system; therefore, whether a provision is revenue losing is determined by reference to present law. This principle will lead to two important limits on the application of the line item veto to revenue-losing tax provisions.

First, an exception to a new tax being imposed by the Congress does not constitute a revenue-losing provision because the exception does not lose revenue relative to present law. Such a provision, therefore, would only be identified as a limited tax benefit if it meets the definition of a temporary or permanent transitional rule.

Second, the Act will be difficult to apply in the case of a proposed complete restructuring of the Federal tax system. Although the Joint Committee staff believes that whether a provision constitutes a revenue-losing provision should be measured relative to the present-law revenue baseline, that baseline has little relevance in the case of a proposal to restructure the Federal tax system. Thus, the Joint Committee staff believes that it may be necessary to reconsider the application of the line item veto to tax restructuring legislation. Furthermore, the Act only applies to provisions amending the Internal Revenue Code of 1986. The Congress might rename the Code in the process of restructuring it, thus potentially making the Act inapplicable as it relates to limited tax benefits in any future legislation.

Exceptions to revenue-losing provisions

The most difficult task for the Joint Committee under the statute likely will be evaluating whether a provision is not subject to the line item veto because of the statutory exceptions provided by the Act. Neither the statute nor the legislative history provide any significant guidance as to the intent of the Members with respect to how these exceptions should be interpreted.

There is virtually no guidance in the legislative history of the Act with respect to the standards that should be applied in determining whether beneficiaries of a tax benefit are eligible for one of the exceptions. The Joint Committee staff believes that common sense dictates an interpretation of the exceptions that does not cause the substantive rule to have no effect. Thus, the Joint Committee staff intends to apply general principles that (1) can be applied consistently to varying types of provisions and to the various exceptions, and (2) can be justified as a reasonable interpretation of the Congressional intent to apply the line item veto in a fairly

specific and narrow manner. The determination of whether a particular provision is a limited tax benefit necessarily will be a fact and circumstances determination.

Transitional relief

The limited tax benefit definitions with respect to transitional relief differ from those governing revenue-losing provisions in two principal respects. First, the threshold number of beneficiaries necessary to avoid limited tax benefit classification is lower for transitional relief than for a revenue-losing provision. Transitional relief cannot be a limited tax benefit if it benefits more than 10 beneficiaries; while a revenue-losing provision cannot be a limited tax benefit if it benefits more than 100 beneficiaries.

Second, a revenue-losing provision is not a limited tax benefit, even if it affects a small number of beneficiaries (such as 10 or fewer) if the provision falls within certain categories, generally such that all persons in the same industry, engaged in the same activity, or owning the same type of property receive the same treatment. There are also exceptions for treatment that differs as a result of size, demographic conditions, amounts involved, or a general election provided under the Code. The statute does not provide any such exceptions in the case of transitional relief.

A number of difficult issues are expected to arise because the line item veto legislation distinguishes "transitional relief" from other situations that may appear to involve a relative benefit for a small group of taxpayers. In general, it will be necessary to determine when an exception from a change in law should be considered "transitional relief" as opposed to part of the basic scope and structure of the new law. This determination may be particularly difficult in situations that might be deemed to involve permanent transitional relief.

In applying the line item veto law, the Joint Committee staff will treat a provision as transitional relief if it refers to a "closed" class of taxpayers. A class will be considered "closed" if other taxpayers engaging in the same transaction or activity, or using the same type of property or engaging in the same industry, in the same time period, will not be able to benefit from the rule because the rule identifies eligible taxpayers in a manner that is or will become impossible for others to meet. If a provision is expected as a practical matter to benefit a fixed class of taxpayers, the Joint Committee staff will also consider this to be a factor. In other limited circumstances, factors other than the existence of a closed class also may indicate that a provision is transitional relief.

The Joint Committee staff will apply an analysis that permits a provision to be treated as "transitional relief" even if it does not precisely retain prior law, where necessary to prevent avoidance of the apparent purpose of the transitional relief rules. In some instances, a revenue-losing provision may also be considered to provide transitional relief. In such cases, the provision will be analyzed under the rules relating to revenue-losing provisions as well as the rules relating to transitional relief, and will be a limited tax benefit if it would be so classified

under either set of rules. A revenue-raising provision also may be considered "transitional relief" if it retains a part of prior law in the context of a broader change.

III. DISCUSSION OF SPECIFIC ISSUES

A. Definition of a Provision

Approach to defining provision

The definition of a "provision" is relevant both in determining whether an item is a limited tax benefit because it is a "revenue-losing provision" and in determining whether an item is a limited tax benefit because it is a "Federal tax provision which provides temporary or permanent transitional relief." The definition of "provision" is the same with respect to both types of limited tax benefit. Neither the statutory language nor the legislative history of the Act define the term "provision;" however, use of the word "provision" in the statute rather than the word "section" indicates that it was not intended that the sections of the bill be determinative of what is a provision.

The Joint Committee staff will consider the substance of specific legislative language in identifying whether an item is a "provision," rather than applying a standard that looks merely at whether statutory language is within the same section, subsection, paragraph, or clause of a bill. Thus, for example, a particular phrase in a subsection of a bill may be considered a provision. Similarly, two related items in two separate sections may be considered a single provision. Such an approach is consistent with the statutory use of the term "provision" and the Joint Committee staff's overall approach of looking at the substance of legislation rather than the form. It will also help to reduce the circumstances in which the line item veto legislation can be avoided by drafting.

The statutory language and the legislative history make it clear that the line item veto legislation was not intended to give the President the authority to modify or rewrite provisions, only to strike out provisions. The Joint Committee staff will not consider an item a "provision" unless it consists of language that can be separately stricken without otherwise having substantive effect. If, after the language is stricken, the remaining language would require modification in order to be comprehensible or would have a different substantive effect (beyond removal of the limited tax benefit), then the language proposed to be stricken would not be considered a provision.

There may be some circumstances in which a provision may be drafted so that it is not a limited tax benefit, whereas it would be a limited tax benefit if it were drafted differently. That is, in some cases, items in a bill may be drafted so that it is not possible to strike separately language that confers a limited tax benefit because the remaining language would require modification to remain comprehensible.

For example, a single numbered section of the Small Business Job Protection Act of 1996 contained two subsections with provisions relating to fisherman. One provision was a revenue-losing provision that modified a rule relating to the employment tax treatment of certain fishermen. The other provision, a revenue-raising provision, modified reporting requirements

relating to certain purchases of fish.[29] Even though these two items are in the same section of the Act, they would be considered separate provisions for line item veto purposes; they are not explicitly connected statutorily. The employment tax provision, if determined to be a limited tax benefit,[30] could be separately stricken. On the other hand, assume that the reporting provision contained separate language stating that it would not be effective unless the employment tax provision were effective (i.e., was enacted and not stricken pursuant to the line item veto). Further assume that the employment tax provision were in fact a limited tax benefit (i.e., it was revenue-losing, benefited 100 or fewer beneficiaries, and no exceptions applied). For purposes of the line item veto rules, the employment tax provision and the separate language conditioning the enactment of the reporting requirement on enactment of the employment tax provision would be treated as a targeted tax benefit for purposes of the Act. Thus, if the President exercised his cancellation authority with respect to the employment tax provision and the Congress did not disapprove the cancellation, the employment tax provision would not be effective, but the reporting requirement would be. Note, it might be possible to draft the two provisions in such a manner that the revenue-losing provision could not be stricken without also affecting the reporting requirement. In such a case, the employment tax provision would not be considered a separate provision for purposes of the line item veto.

The revenue estimates prepared by the Joint Committee staff in conjunction with the consideration of legislative proposals are not determinative of whether items are provisions for purposes of the line item veto, unless the estimate has been specifically prepared for such purpose. That is, for line item veto purposes, an item may be considered a separate provision even if it is not separately estimated on revenue tables prepared by the Joint Committee staff for the use of Members and committees in considering proposed legislation. Similarly, items for which separate estimates are provided may not be considered separate provisions for purposes of the line item veto legislation.

Limited tax benefits involve provisions that change the Internal Revenue Code

The Act provides that a provision is a limited tax benefit if it is a revenue-losing provision that provides benefits under the Code or if it provides permanent or temporary transition relief from a change to the Code. Thus, an item may be considered a limited tax benefit for purposes of the Act only if it amends the Code (directly or indirectly). A provision that is estimated to lose revenue will not be considered a revenue-losing provision under the Act unless the revenue loss is due to a change (direct or indirect) to the Code.

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[29] The employment tax provision is in section 1116(a) of the Small Business Job Protection Act of 196, and the reporting provision is in section 1116(b).

[30] This provision would not be a limited tax benefit in any event. It is estimated to benefit more than 100 beneficiaries.

For example, suppose a provision provides that, notwithstanding any other provision of law, a certain group of companies is entitled to deduct 100 percent of meals and entertainment expenses. This might be considered a limited tax benefit provision for purposes of the Act, because it indirectly amends the section of the Code that limits the deduction for meals and entertainment expenses to 50 percent. The fact that the amendment is accomplished without a specific reference to the Code is immaterial. On the other hand, suppose a provision amends the Federal labor laws to provide that employer-provided health plans are required to meet certain requirements as to the amount and types of coverage provided. Such a requirement may be estimated to have a revenue effect because it may affect the amount of taxable and nontaxable wages received by employees. Even if the provision were estimated to lose revenue, it would not be considered a revenue-losing provision under the Act because the revenue loss is not a result of a change (direct or indirect) to the Code.[31]

B. Determination of the Number of Beneficiaries

Statutory incidence defines "beneficiary"

The Act defines a limited tax benefit by reference to revenue losing a provision that affects "100 or fewer beneficiaries under the Internal Revenue Code"[32] or provisions that provide temporary or permanent transitional relief to "10 or fewer beneficiaries" from a change to the Internal Revenue Code.[33] However, neither the statute nor the Statement of Managers define the term "beneficiary" of a limited tax benefit. Conversely, the Internal Revenue Code does define the term "taxpayer" to mean the person liable for payment of tax.[34] The Joint Committee staff will interpret the term "beneficiary" by its most plain meaning, that is, the taxpayer who is entitled to the "deduction, credit, exclusion, or preference."[35] The approach of the Joint Committee staff generally will follow the statutory incidence of the tax imposed by the Internal Revenue Code and the legislation under review in defining "beneficiary." Indeed, the use of

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[31] An example of such a provision is the recently enacted provision requiring health insurance to cover 48-hour maternity stays. This provision was estimated to have a revenue effect, even though there was no direct or indirect amendment to the Code. (This provision would not be a limited tax benefit even if a change to the Code were involved, because it benefits more than 100 beneficiaries.)

[32] New section 1026(9)(A)(i) of the Budget Act.

[33] New section 1026(9)(A)(ii) of the Budget Act.

[34] Code section 7701(a)(14). In most cases, the person who remits the cash to the Treasury is the person liable for the tax. Two exceptions to this are the communications excise tax and the air ticket taxes.

[35] New section 1026(9)(A)(i) of the Budget Act.

statutory incidence of the tax is most consistent with the special rules provided in the Act that aggregate beneficiaries in certain circumstances (discussed below).

Special rules in defining beneficiaries

The Act provides the following four special rules for identifying and measuring the number of beneficiaries in certain circumstances:[36]

(1) All businesses and associations which are related (within the meaning of Internal Revenue Code sections 707(b) and 1563(a)) are to be treated as one beneficiary;
(2) All qualified plans of a single employer are to be treated as one beneficiary;
(3) All holders of the same bond issue are to be treated as one beneficiary; and
(4) Individual shareholders of a corporation, partners of a partnership, members of an association, or beneficiaries of a trust or estate are not to be counted as separate beneficiaries if a benefit is provided to the respective corporation, partnership, association, trust, or estate .

These exceptions generally have the effect of aggregating what otherwise might appear to be numerous beneficiaries into one.

The first aggregation rule is an anti-avoidance rule. For example, it would be inconsistent with the intent of the Act if a corporation could create multiple subsidiaries and thereby exceed the 100-beneficiary threshold. Similarly, the Internal Revenue Code employs related-party rules and other aggregation rules to insure that a Code provision cannot be circumvented by taxpayers altering their legal form. The second aggregation rule is similar to the first in that the creation of multiple qualified plans by a single employer does not enable the qualified plans to exceed the 100-beneficiary threshold.

The third aggregation rule clarifies the application of the beneficiary definition in a case where it could be argued that statutory benefits are granted to multiple persons by one tax provision. For example, under conditions prescribed by the Code (secs. 103 and 141-149), State and local governments may issue tax-exempt bonds, securing for themselves the benefit of tax-exempt financing. At the same time, purchasers of such bonds may exclude such interest income from their gross income (Code sec. 103). In the absence of an aggregation rule, it may be ambiguous whether a provision permitting a single State to issue additional tax-exempt bonds constitutes a limited tax benefit, as one could argue under sections 141 through 149 that only one issuer was benefitting or, alternatively, one could argue under section 103 that numerous bondholders were benefitting.[37] The most clear statutory reading may be that qualified bonds

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[36] New section 1026(9)(D) of the Budget Act.

[37] This aggregation rule also may serve specifically to identify provisions of a type which in the past were recognized as providing limited tax benefits or limited transition relief. For example, see sections 1317(3)(A)-(Y) of the Tax Reform Act of 1986. These transition rules generally are recognized as permitting the interest paid by specific bond issuers to qualify under

have interest that is exempt under section 103; hence, the statutory incidence lies with the bondholders, of which there might be many. The specific aggregation rule of the Act treats all bondholders of the same bond issue as one for the purpose of determining the number of beneficiaries.

The fourth aggregation rule is aimed at treating similarly situated taxpayers equivalently. In general, under this rule, if a benefit is provided at the entity level, the entity is treated as the beneficiary, even if it is not a separate taxpayer. The rule treating partners in a partnership or shareholders of an S corporation as a single beneficiary is contrary to their positions as taxpayers but treats business entities established as a partnership or S corporation equivalently to those established as C corporations. Thus, for example, an exception granted to a single partnership from general partnership information reporting requirements would be counted as an exception granted to one beneficiary (the partnership) regardless of the number of partners in the partnership. The rule requiring shareholders of a corporation to be treated as one in the case of a benefit provided to a C corporation appears redundant, as the principle of statutory incidence would conclude that a single C corporation, and not its shareholders, is the statutory taxpayer. The rule, however, clearly has meaning in the case of S corporations. The need for the rule is less clear in the case of trusts and estates as most trusts and estates are statutory taxpayers. It should be noted that the fourth aggregation rule applies only in the case of a benefit granted to the entity; this fourth aggregation rule does not aggregate all shareholders or partners for all purposes (see further discussion below).

Federal, State, and local governments as beneficiaries

The Federal Government generally is exempt from the provisions of the Internal Revenue Code, with the exception of the vaccine excise tax and air ticket and air freight taxes. The Joint Committee staff will not consider the Federal Government to be a beneficiary for the purpose of determining the number of beneficiaries.

Unlike the Federal Government, State and local governments and Indian tribes may be subject to the payroll tax and certain excise taxes.[38] State and local governments and Indian tribes may be beneficiaries for the purpose of determining the number of beneficiaries.

Determination of relevant fiscal years

The Act requires that the number of beneficiaries be determined "in any fiscal year for which the provision is in effect"[39] in the case of a revenue-losing provision and "in any fiscal

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section 103 of the Internal Revenue Code.

[38] Indian tribes and certain educational institutions of state and local governments also may be subject to tax on unrelated business income on certain activities.

[39] New section 1026(9)(A)(i) of the Budget Act.

year"[40] in the case of temporary or permanent transitional relief. As a practical matter, it will be impossible to determine with any reliability the number of beneficiaries of a provision in fiscal years many years after the first fiscal year for which a provision is in effect. Thus, the Joint Committee staff will adopt a rule of convenience in determining whether the number of beneficiaries of (1) a revenue-losing provision totals 100 or fewer in any fiscal year for which the provision is in effect or (2) a provision providing permanent or temporary transitional relief totals 10 or fewer in any fiscal year. Under this rule of convenience, the Joint Committee staff generally will determine the number of beneficiaries of a provision for any relevant fiscal year for which the Joint Committee staff also is providing a revenue estimate for the provision.

Under the Budget Act, the Joint Committee on Taxation is required to provide revenue estimates for revenue provisions for the budget year and the following four fiscal years covered by a concurrent resolution on the budget. Senate rules provide a point of order for any revenue legislation that would increase the deficit in any of the following three periods: (1) the first fiscal year covered by the most recent budget resolution, (2) the first five fiscal years covered by the most recent budget resolution, and (3) the second five fiscal years covered by the most recent budget resolution.

Because the Joint Committee typically is required to provide revenue estimates under Senate rules for at least 10 years, the Joint Committee staff generally will evaluate whether the 100 or fewer beneficiaries standard for revenue-losing provisions (or the 10 or fewer beneficiaries standard for permanent or temporary transitional relief) is satisfied by determining the number of beneficiaries for any year during the normal estimating period that a provision is in effect. Therefore, the Joint Committee staff will generally determine the number of beneficiaries of a provision for each of the 10 fiscal years commencing with the first fiscal year covered by the most recent budget resolution.

If a provision is not in effect for all of such 10 fiscal years, then the number of beneficiaries will be determined for each of the fiscal years that the provision is in effect within such 10 fiscal year period. However, the number of beneficiaries will be determined over no less than a five fiscal year period beginning with the fiscal year in which the provision becomes effective. For example, if a revenue-losing provision is not scheduled to become effective until after the fifth year of the typical Joint Committee revenue estimating period, then the Joint Committee staff will determine whether the 100 or fewer beneficiaries standard (or the 10 or fewer beneficiaries standard) is satisfied in any of the five consecutive years that begin with the fiscal year in which the provision becomes effective.[41] Thus, if the first fiscal year covered by the most recent budget resolution were 1998 and a provision were enacted to become effective in

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[40] New section 1026(9)(A)(ii) of the Budget Act.

[41] See the discussion in Part C.1., below, relating to the first fiscal year for which a provision is effective.

fiscal 2004, the Joint Committee staff would test the provision against the number of beneficiaries standards for the fiscal years 2004 through 2008.

A tax provision could be viewed as being "in effect" in those fiscal years in which taxpayers are entitled to claim the deduction, credit, or other tax preference. Alternatively, a provision could be viewed as being "in effect" in those fiscal years in which the tax preference actually results in a reduction in tax receipts to the Treasury.[42] The Joint Committee staff believes that the intent of Congress can best be followed by viewing a tax preference as being in effect in any fiscal year in which taxpayers are entitled to claim the tax preference or use the tax preference to reduce tax liability. Thus, for example, a tax credit will be viewed as being in effect in those fiscal years in which taxpayers are entitled to claim credits and those fiscal years in which taxpayers may use the credits to reduce their tax payments.

Counting beneficiaries

A taxpayer will be counted as the beneficiary of a tax preference in those fiscal years in which the taxpayer uses the tax preference to reduce tax payments. For example, if a taxpayer is entitled to claim a tax credit in fiscal year 1997, but the taxpayer's situation is such that the taxpayer must carry the credit forward unused, the taxpayer will not be counted as a beneficiary in 1997. If the same taxpayer carries the credit forward and uses the credit to reduce his tax payments in fiscal year 1999, the taxpayer will be counted as a beneficiary in fiscal year 1999 (but the taxpayer will not be counted as a beneficiary in fiscal year 1998).

As an illustration of the rules for counting beneficiaries and determining the fiscal years when a provision is in effect, the Small Business Job Protection Act of 1996 ("Small Business Act") included a provision creating the work opportunity tax credit ("WOTC"), which is effective for employees hired during the period October 1, 1996, through September 30, 1997. It is estimated that several thousand employers will be entitled to claim the WOTC during this one-year period. However, some of the employers earning the credits will be subject to the alternative minimum tax and will have unused credits that they will carry forward and claim in future tax years. As a result of credits carried forward, it is estimated that the one-year reinstatement of the credit will lose revenue in each of the fiscal years 1997 through 2002. It is estimated that the revenue loss in fiscal year 2002 will be attributable to carry forward credits claimed by 100 or fewer employers. The Joint Committee staff would view the WOTC as being in effect in fiscal year 2002, with 100 or fewer beneficiaries in that fiscal year. Thus, the Joint Committee staff would identify the WOTC provision as benefiting 100 or fewer taxpayers in at least one year in which it is in effect. In this example, the identification of the Small Business

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[42] A taxpayer cannot always use a deduction, credit, or other preference to reduce tax liability in the year he is entitled to claim such deduction, credit, or preference. For example, insufficient taxable income in the current year may result in the taxpayer carrying a credit forward to a future taxable year at which time he utilizes the credit to reduce his tax liability in that future year.

Act's WOTC provision as benefiting 100 or fewer taxpayers is a result of the fact that the provision creates a temporary credit. If the credit had been enacted as a permanent provision, it would have benefitted several thousand taxpayers in each year of the relevant period, exceeding the 100 or fewer beneficiary threshold throughout the relevant period.

To make revenue estimates of proposed legislation, the Joint Committee staff frequently must estimate the number of taxpayers affected by changes in tax provisions. Sometimes such estimates are based on the examination of past tax returns. At other times, other data sources are used. The Joint Committee staff anticipates that it will estimate the number of beneficiaries using the best available data and statistical practice as it does in fulfilling its current revenue estimation obligations under the Budget Act.[43]

Issues in determining the number of beneficiaries

Alternative approach to statutory incidence.-- An alternative view of the definition of beneficiary would be to use the economic incidence of a provision. For example, manufacturers' excise taxes are levied statutorily on the manufacturer, but economists often conclude that such taxes largely are borne ultimately by the consumers of the taxed products through a change in the products' prices. Using statutory incidence, a manufacturer would be the beneficiary of a reduction in a given excise tax. Using economic incidence, the consumers of the products would be the beneficiaries of a reduction in the same excise tax.

There are two substantial impediments to adopting economic incidence as the standard for determining the beneficiaries of a provision. First, it requires an estimate of the economic incidence of the tax. There can be uncertainty to such estimates. For example, is the burden of a given tax borne by the consumers of products or the producers of products and, if by producers, by the owners of the firm's capital or by the firm's laborers? In cases in which the long-run economic incidence differs from the short-run economic incidence, which analysis would be most relevant to the provision in question?[44] In cases in which the economics profession offers no consensus or no guidance as to the economic incidence of a tax benefit, the Joint Committee staff might appear to be making an arbitrary judgment as to the economic incidence. By comparison, the statutory incidence generally is easily and clearly identified.

In many cases, using the standard of economic incidence might vitiate the intent of the Act. The large scale of the United States' economy may make it unusual for an analysis of economic incidence to identify 100 or fewer taxpayers benefitting from a tax preference. For

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[43] See also the discussion in Part C.1., below, relating to the definition of revenue-losing provision.

[44] See, Joint Committee on Taxation, *Methodology and Issues in Measuring Changes in the Distribution of Tax Burdens* (JCS-7-93), June 14, 1993, for a discussion of practical difficulties and uncertainty in economic incidence analysis.

example, assume a provision created a tax preference for one company. In any case in which the economic incidence of the tax preference falls on consumers of the product or employees of the company (or both), it likely would be the case that more than 100 individuals would benefit. As a further illustration, the 1913 statute creating the Federal income tax provided an exemption for the then sitting President, Woodrow Wilson.[45] In statutory terms, this clearly fits the definition of a limited tax benefit with one beneficiary. However, a general equilibrium economic analysis could suggest that there were substantially more beneficiaries. Because of the tax exemption, President Wilson may have consumed more goods and saved more than he otherwise would. His purchases of goods would create small, but nonzero, additional profits for the firms he patronized. His purchases also may have created additional work effort and small, but nonzero, increases in the earnings of the employees of those firms. Likewise, President Wilson's increase in saving may have provided the basis of a bank loan to other firms expanding their scale. The "second round" effects, though quite small, could easily affect more than 100 taxpayers. If this type of analysis were employed, using a standard of economic incidence would result in provisions rarely being identified as limited tax benefits. Such an outcome seems counter to Congressional intent in including certain limited tax benefits as part of the President's line item veto authority.

Limitations created by the choice of statutory incidence.--Whether or not a provision constitutes a limited tax benefit may depend on the statutory incidence of the provision. For example, assume the Motor Kar Corporation of America ("MKCA") manufactures and sells annually approximately 300 special cars of one model called the "SportsKar." Further assume Congress wanted to provide a tax benefit for the purchase of the SportsKar. There is only one manufacturer of such vehicles, MKCA, but there are 300 purchasers per year. The Congress could provide a $10,000 income tax credit to MKCA for each car sold or the Congress could provide a $10,000 income tax credit to the buyer of each SportsKar purchased. Economic analysis establishes that it does not matter who gets the credit, the economic incidence is the same.[46] Using a statutory incidence standard, who is entitled to claim the credit will determine whether or not the provision is a limited tax benefit. If it is a manufacturers' credit, then the Joint

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[45] This is an example of transitional relief and a standard of 10 or fewer taxpayers would apply. See Part IV.B., for discussion of this example.

[46] See, for example, the analysis in Richard A. Musgrave and Peggy B. Musgrave, *Public Finance in Theory and Practice*, Fourth Edition (New York: McGraw-Hill Book Company), 1984, p. 270; Harvey S. Rosen, *Public Finance*, Second Edition (Homewood, Illinois: Irwin), 1988, p. 271; and Joseph E. Stiglitz, *Economics of the Public Sector* (New York: W. W. Norton & Co.), 1986, p. 352.

This theoretical example disregards the issue whether the buyers or the sellers have sufficient tax liability to claim such a credit. Such factors may affect the general economic conclusion that the incidence of a tax or tax benefit is the same whether statutorially granted to the producer or consumer of a product.

Committee staff would identify this credit as a limited tax benefit, as one taxpayer, MKCA, is entitled to a tax credit. If it is a purchaser's credit, then the Joint Committee staff would not identify this credit as a limited tax benefit as 300 taxpayers would be entitled to a tax credit each year. Thus, drafting the credit as a purchasers' credit rather than a manufacturer's credit would cause the provision not to be identified as a limited tax benefit.

Issues in applying aggregation rules.--The aggregation rules provided by the Act are limited in scope. For example, the rule aggregating qualified plans does not treat all plan beneficiaries as a single beneficiary of a plan. If XYZ Corporation had established more than 100 qualified plans, a provision exempting the plans of XYZ Corporation from certain compliance measures would be treated as affecting one beneficiary (the aggregated plans of XYZ Corporation.) However, a provision that exempted the distributions from one of the plans to retired employees of XYZ Corporation from income tax would not be identified as a limited tax benefit if there were more than 100 such recipients of the distributions because the recipients are the statutory taxpayers affected by the provision.

The aggregation rules do not address whether all employees of a single employer should be counted as one beneficiary for certain purposes. For example, assume XYZ Corporation provides each of its 1,000 employees with parking valued in excess of the limitation provided under Code section 132(f)(2)(B) and, therefore, such excess value is included in the employees' gross income. Further assume that Congress votes to exempt the employees of XYZ Corporation from tax on the excess value of parking provided not withstanding the section 132 limitation. XYZ Corporation may deduct expenditures to provide employee parking as necessary business expenses regardless of whether any such amounts are includible in the employees' incomes under section 132. The statutory beneficiaries in this example would be the 1,000 employees of XYZ Corporation.[47] Under the principle of statutory incidence, because there are more than 100 employees of XYZ Corporation, the Joint Committee staff would not identify this provision as a limited tax benefit. If such an outcome is not consistent with Congressional intent in enacting the Act, a technical correction may be required.[48] A rule aggregating all plan beneficiaries as one or all employees as one may be desirable and consistent with the bondholder aggregation rule, but it an amendment to the Act would be required to achieve such a result.

Likewise, the aggregation rules do not treat all shareholders of a corporation as one in the case where a benefit is provided to the shareholders of the corporation. For example, assume a provision provided that any taxpayer receiving dividends from ABC Inc. could exclude those

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[47] The hypothetical provision also would lower the payroll tax liability of XYZ Corporation. See the specific example below relating to employer and employee liability for payroll taxes.

[48] An additional question would arise as to whether, if it were decided to aggregate all employees of an employer as one beneficiary, it would be appropriate to count an employer and its employees as two beneficiaries or as one beneficiary.

dividends from gross income. If the shareholders of ABC Inc., who otherwise would be liable for taxes on dividends paid by ABC Inc., numbered more than 100, the Joint Committee staff would not identify this as a limited tax benefit. To treat all shareholders of one corporation as one beneficiary would require an amendment to the Act. Such a rule would be consistent with the bondholder aggregation rule.

The absence of an aggregation rule may place more importance on the form in which a tax benefit is proposed. For example, the Omnibus Budget Reconciliation Act of 1993 created a tax credit for contributions by taxpayers to certain qualifying community development corporations.[49] The number of qualifying organizations, which were established under the current law relating to such organizations, was less than 100. However, the likely number of contributors might number more than 100. In evaluating the statutory incidence of the provision, the Joint Committee staff might calculate that there would be more than 100 contributors benefitting from the credit, even though fewer than 100 organizations would be receiving the donations. To aggregate all donors to a specific charitable organization would require an amendment to the Act.

Cases in which there is more than one statutory beneficiary.--In some cases, there may be more than one statutory beneficiary. In such cases, the Joint Committee staff will count all beneficiaries in determining whether the applicable threshold has been exceeded. For example, under present law, there is no exclusion from gross income or for employment taxes for employer-provided group legal services. Suppose a provision states that if certain companies provide group legal services, the value of such services is excludable from income for income and employment tax purposes. In this case, the employees of the companies would be beneficiaries, because they receive a benefit in the form of an income and employment tax exclusion. In addition, the companies providing the group legal services also would be beneficiaries; they benefit from lower payroll tax liability. For purposes of determining whether there are 100 or fewer beneficiaries, the Joint Committee staff would count both the employees of the companies and the companies themselves, because all are statutory beneficiaries of the provision.

As described above, the special aggregation rules may be interpreted as clarifying certain instances where a limited tax benefit might be found to exist if the definition is applied with respect to one provision of the Code, but not with respect to another. The Act did not address certain other similar situations. For example, consider a provision that expands the class of public charities (as defined by section 509) to include one organization that was previously considered to be a private foundation. Changing the definition of private foundation in Section 509 in this manner creates a benefit to that organization by exempting its net investment income from the two-percent excise tax imposed under section 4940. Thus, the provision expanding the class of public charities might be interpreted to be conferring a limited tax benefit. However, by changing the definition of private foundation in Section 509 in this manner, potential

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[49] Section 13311 of Omnibus Budget Reconciliation Act of 1993.

contributors to that public charity also benefit. Gifts to public charities are subject to more favorable deduction rules than are gifts to private foundations. Hence, the provision that expands the class of public charities may grant more than 100 contributors a tax benefit. As discussed above, unlike the case of bondholders, an aggregation rule is not applied to treat contributors to a charitable organization as a single beneficiary. Under present law, a taxpayer may deduct contributions to qualified organizations. Creating a new organization that qualifies as a public charity does not require an amendment to section 170 or section 4940. Following the principle of statutory incidence, the taxpayers affected by the statutory change would be the organization whose private foundation status was changed and any contributors to such an organization. If contributors numbered 100 or more annually, in the absence of an aggregation rule, the Joint Committee staff would not identify this provision as creating a limited tax benefit.

C. Revenue-Losing Provisions that Benefit 100 or Fewer Beneficiaries

1. Definition of revenue-losing provision

In general

A revenue-losing provision is any provision that is expected to result in a reduction in Federal tax revenues in (1) the first fiscal year in which the provision is effective, or (2) the 5-year period beginning with the first fiscal year in which the provision is effective. The revenue effects of a provision are estimated by comparing the forecast of revenues that would be collected under present law with the forecast of revenues that would be collected if the provision were enacted.

Each January, the Congressional Budget Office ("CBO") prepares a detailed forecast of the Federal tax revenues that will be collected in the current fiscal year and each of the next 10 fiscal years if present law remains unchanged. This forecast is referred to as the "CBO baseline." The Joint Committee staff is responsible for estimating the changes in tax revenues that would result from the enactment of various tax proposals under consideration by the Congress. If the Joint Committee staff estimates that a tax provision will reduce tax revenues below CBO baseline revenues in the first fiscal year or first 5 fiscal years in which the provision is effective, then the provision will be viewed as a revenue-losing provision for purposes of the Act, regardless of the size of the expected revenue loss.

The Act does not contain a de minimis exception for revenue-losing provisions that lose only a small amount of revenue. Thus, an expected revenue loss of even a very small dollar amount would be sufficient to cause a provision to be a revenue-losing provision. Joint Committee revenue tables will sometimes indicate that a specific tax provision will have a "negligible" effect on Federal tax receipts in a particular fiscal year or group of fiscal years. This should be interpreted as an indication that the provision will have a negligible effect on revenues (either positive, negative, or indeterminate) from the perspective of the Treasury, not an indication that the provision is not a revenue-losing provision for purposes of the Act. For example, a tax provision that is expected to lose $400,000 of revenue in the current fiscal year

might be listed as having a "negligible" effect on revenues in a Joint Committee revenue table, but would be considered to lose revenue for purposes of the Act.

There are a number of ways in which a tax provision could reduce Federal tax revenues in a given fiscal year. For example, a provision could reduce the tax rate or narrow the tax base, and thereby reduce tax liabilities, or it could delay the timing of required tax payments, and shift some tax payments into the following fiscal year. A tax provision also could reduce reporting requirements for certain transactions, and thereby reduce tax compliance. Any tax provision that reduces Federal tax revenues in one or more fiscal years has the potential to be a revenue-losing provision, regardless of the source of the revenue loss.

Interactions among provisions

If a bill contains two or more tax provisions, there may be interactions among the provisions. When there are interactions, a tax provision may have differing revenue effects depending upon whether it is viewed relative to present law or relative to the law that would exist if the remaining tax provisions in the bill were enacted. In determining whether a provision is a revenue-losing provision for line item veto purposes, the revenue effects of the provision must be estimated relative to present law. Thus, each tax provision in a tax bill must be viewed in isolation.

Consider, for example, a bill that would (1) shift certain computer equipment from the 5-year property class to the 3-year property class for depreciation purposes and (2) prohibit the expensing of any 3-year property under section 179. When viewed relative to present law, the provision that reclassifies computer equipment as 3-year property would be scored as a losing revenue. However, when viewed in conjunction with the provision prohibiting expensing of 3-year property, the reclassification of computer equipment as 3-year property might be scored as raising revenue. For line item veto purposes, the provision reclassifying computer equipment as 3-year property would be scored relative to present law, and thus would be considered a revenue-losing provision.

Exception to new taxes

In general, an exception to a new tax will not be considered a revenue-losing provision, because it will not lose revenue relative to present law. Consider, for example, a bill that would (1) levy a new general excise tax on automobile manufacturers and (2) provide an exemption from the new excise tax for manufacturers of electric automobiles. The exemption would need to be scored relative to present law to determine whether it is a revenue-losing provision for line item veto purposes. Because present law contains no general excise tax on automobile manufacturers, the exemption would not be viewed as a revenue-losing provision. However, the exemption might be a limited tax benefit if it satisfies the definition of a provision which provides temporary or permanent transitional relief. Note that if the exemption were enacted as part of a separate bill after the enactment of the excise tax on automobile manufacturers, the

excise tax would be viewed as a part of present law and the exemption would be viewed as a revenue-losing provision.

If a tax bill provides for a major restructuring of the Internal Revenue Code (or a portion of the Code), then it might be difficult to estimate the revenue effects of the individual provisions of the bill relative to present law. It might be determined that the individual provisions have no meaning in the context of present law. Thus, the Joint Committee staff believes that it may be necessary to reconsider the application of the line item veto to tax restructuring proposals.

First fiscal year

As a part of the process for determining whether a provision is a revenue-losing provision, it is necessary to identify the first fiscal year in which the provision will be effective. In general, the first fiscal year will be (1) the fiscal year containing the effective date of the provision, or (2) in the case of a retroactive provision, the fiscal year containing the date of enactment. If a provision is retroactive or is drafted so that it will become effective on the date of enactment, the Joint Committee staff's assumed date of enactment for estimating purposes will be used.

The following examples illustrate the rules for determining the first fiscal year in which a provision is effective. It is assumed that all of the following provisions are contained in a bill that is in conference in late September 1997 and is expected to be enacted on October 1, 1997:

--An income tax provision in the bill is effective for taxable years beginning on or after the date of enactment. Fiscal year 1998 will be viewed as the first fiscal year in which the provision is effective because that is the fiscal year in which enactment is assumed to occur.

--An income tax provision in the bill is effective for taxable years beginning on or after January 1, 2002. Fiscal year 2002 will be viewed as the first fiscal year in which the provision is effective because that year contains the effective date.

--An income tax provision in the bill is effective for taxable years beginning on or after January 1, 1995. Fiscal year 1998 will be viewed as the first fiscal year in which the provision is effective because the provision is retroactive and fiscal year 1998 is the year in which enactment is assumed to occur.

If it is expected that a tax provision will be enacted in late September of the current fiscal year, effective on date of enactment, then the current fiscal year will be viewed as the first fiscal year in which the provision is effective. However, the tax provision may be scored as having no revenue effect in the current fiscal year because there is insufficient time for tax payments or tax refunds to be affected. If this is the case, the tax provision will not be viewed as a revenue-losing provision unless it results in a revenue loss in the 5-year period beginning with the current fiscal year.

Most tax provisions become effective upon enactment or soon thereafter, but in certain circumstances the Congress may wish to consider a tax provision that will not become effective until a year or more after enactment. Joint Committee staff revenue estimates that cover the normal 10-year estimating period will not be sufficient for the evaluation of potentially revenue-losing tax provisions that will not become effective until after the sixth year of the estimating period. If a tax provision is a potential revenue-losing provision, then the Joint Committee staff will prepare a revenue estimate for the provision that covers the first fiscal year in which the provision is effective and the 4 subsequent years, regardless of whether these years fall within the normal 10-year estimating period.

Revenue losses and beneficiaries

A revenue-losing provision is a limited tax benefit if it "provides a Federal tax deduction, credit, exclusion, or preference to 100 or fewer beneficiaries." In most cases in which a revenue-losing provision qualifies as a limited tax benefit, the revenue loss will be directly attributable to a reduction in tax payments by the 100 or fewer beneficiaries. However, the Act does not require that the revenue loss be directly attributable to the 100 or fewer beneficiaries who receive the tax deduction, credit, exclusion, or preference. In some cases, the entire revenue loss will be attributable to taxpayers other than the statutory beneficiaries.

Consider, for example, a provision to provide an income tax exemption for organizations that provide health insurance risk pooling for high-risk individuals. It might be the case that no such organizations are forecast to exist under present law within the 10-year budget period. The enactment of the tax provision might be assumed to provide a sufficient incentive for such organizations to come into existence. However, the revenue loss that might result from enactment of the provision would not be directly attributable to a reduction in tax liabilities of such organizations, since none are assumed to exist under present law in the budget period. Rather, the revenue loss would be attributable to a reduction in tax payments by the taxable businesses that will earn less income as a result of the competition provided by the organizations providing the risk pooling.

Identification of revenue-losing provisions

During each session of Congress, the Joint Committee staff prepares a large number of revenue estimates in response to requests from Members of Congress and congressional committees. Joint Committee revenue estimates and revenue tables generally are presented in a manner that satisfies the needs of the requesting Member or committee. Separate revenue estimates for the individual pieces of a larger tax proposal may not be provided unless specifically requested. For example, if asked to estimate the revenue effects of a complex proposal for medical savings accounts, the standard procedure of the Joint Committee staff would be to provide a single revenue estimate for the proposal, rather than separate estimates for the individual pieces of the proposal. Joint Committee revenue estimates and revenue tables have the general purpose of showing the budget effects of the tax proposals under consideration, and will not always be suitable for identification of limited tax benefits. Thus, the manner in

which items are presented on a revenue table will not be determinative of whether an item is a limited tax benefit, unless the table was specifically prepared for purposes of the Act.

2. Exceptions

a. General principles

Description of statutory exceptions

The Act provides that even if a provision is determined to be a revenue-losing provision that provides a deduction, credit, exclusion, or preference to 100 or fewer beneficiaries in a given year, such provision will not be a "limited tax benefit" subject to line item veto if the effect of the provision is that (1) "all persons in the same industry or engaged in the same type of activity receive the same treatment" or (2) "all persons owning the same type of property, or issuing the same type of investment, receive the same treatment."[50] In addition, the Act provides that a revenue-losing provision will not be a limited tax benefit if any difference in the treatment of persons under the provision is based solely on "(I) in the case of businesses and associations, the size or form of the business or association involved, (II) in the case of individuals, general demographic conditions, such as income, marital status, number of dependents, or tax return filing status; (III) the amount involved; or (IV) a generally-available election under the Internal Revenue Code of 1986."[51] The Statement of Managers to the Act indicates that the intent underlying these exceptions to the general rule defining a "limited tax benefit" in numeric terms is that a tax provision benefitting 100 or fewer persons should not be subject to line item veto "if the effect of the provision is that all similarly situated persons receive the same treatment."[52]

The legislative history of the Act indicates that there was significant concern among Members of Congress as to the potential scope of these exceptions. For example, Senator Robert Byrd suggested that the same type of property exception might apply to a tax benefit provided to anyone who owned a Rolls Royce because all similarly situated taxpayers (i.e., taxpayers owning Rolls Royce automobiles) would be treated the same.[53]

However, there is virtually no guidance in the legislative history of the Act with respect to the standards that should be applied in determining whether beneficiaries of a tax benefit are similarly situated. Neither the statute nor the legislative history provide any significant guidance as to the intent of the Congress with respect to how these exceptions should be interpreted.

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[50] Section 1026(9)(B)(i) and (ii) of the Budget Act.

[51] Section 1026(9)(B)(iii) of the Budget Act.

[52] House Report 104-191, p. 37.

[53] See floor statement of Senator Byrd at Congressional Record, March 27, 1996, S2961.

The Joint Committee staff believes that common sense and traditional principles of statutory construction dictate an interpretation of the exceptions that does not cause the substantive rule to have no effect. Thus, the Joint Committee staff intends to apply general principles that (1) can be applied consistently to varying types of provisions and to the various exceptions and (2) can be justified as a reasonable interpretation of the Congressional intent to apply the line item veto in a fairly specific and narrow manner. Subject to these principles, the determination of whether a particular provision is a limited tax benefit will necessarily be a facts and circumstances determination.

The Joint Committee staff will utilize the guidelines discussed below to determine whether a provision that provides a benefit to only a limited number of taxpayers nonetheless has an across-the-board effect for similarly situated taxpayers (e.g., within the same industry, or for the same activity or property), such that the provision should not be subject to a separate, line item veto by the President.

Exceptions not satisfied merely by drafting provisions in generic terms

If the statutory exceptions (such as for the "same activity" or "same property") were construed liberally to require only that a provision be written in a generic fashion (i.e., without referring to any particular named taxpayers), then the Act's exceptions could swallow up the general rule that is supposed to subject "limited tax benefits" to the line item veto. For example, if the exception for "same activity" were considered to be satisfied by a provision granting special tax treatment to taxpayers who engage in an activity described in precise detail (and perhaps limited to activity occurring within a particular time period or at a particular geographic site), then the line item veto could not be applied to such a provision drafted in a generic (although highly detailed) fashion on its face, even though the effect would be identical to a tax benefit provision that explicitly names only one beneficiary (or a handful of beneficiaries). Indeed, most of the so-called "rifle-shot" provisions in the 1986 Act were drafted in a generic fashion (i.e., without explicitly referring to the named beneficiary) but the qualifying activity or property was defined in such precise detail that only a few taxpayers qualified for the tax benefit. For example, a tax benefit was provided to anyone who issued bonds in a certain dollar amount on a certain date with respect to a certain project in a particular city -- while, in theory, anyone could have taken the specified action and would be entitled to the benefit, only one issuer could in fact issue such bonds.

It is the view of the Joint Committee staff that Congress did not intend an interpretation under which the line item veto potentially would apply only to those provisions that mention particular taxpayers by name but would not apply to any provision that has the same effect merely because it is drafted in a generic fashion on its face. For this reason, the line item veto statutory scheme specifically requires that the *effect* (as opposed to the form) of a provision must be to provide the same treatment for persons in the same industry or engaged in the same type of activity or owning the same type of property in order for the provision to fall within one of the exceptions to the general rule defining a "limited tax benefit." Therefore, the Joint Committee staff will interpret the statutory exceptions in view of the legislative history referred to above so

that an exception will apply only if the practical effect of a tax provision benefitting 100 or fewer persons is that all similarly situated persons receive the same treatment. In other words, the statutory terms "same industry," "same activity," and "same property" should not be deemed to be satisfied if the tax-preferred industry, activity, or property is so precisely defined (or limited) that the effect of the provision is that similarly situated persons are denied the same tax treatment granted to the benefitted class.

A provision will be considered to benefit all similarly situated taxpayers if the effect of the provision is to equalize the tax treatment of all similarly situated taxpayers. Thus, for purposes of determining whether all similarly situated taxpayers are treated the same under the exceptions, the Joint Committee staff will consider the effect of a provision if the provision were enacted. For example, if a provision makes the treatment of a specified group of taxpayers equivalent to the present-law treatment of all other taxpayers within an industry, or engaged in the same type of activity or purchasing the same type of property, the provision will be treated as providing the same treatment to all similarly situated taxpayers (even though the provision itself changes the tax treatment for only a portion of the taxpayers in an industry, engaged in an activity, or purchasing a type of property). In other words, a provision will not fail to satisfy any of the exceptions if the effect of enacting the provision is to equalize the treatment of all similarly situated taxpayers.

The following guidelines will be used by the Joint Committee staff in determining whether an industry, activity, or enumerated property is described in statutory terms so precise or particular that the effect is that other, similarly situated persons are denied favorable tax treatment (or, in other words, the benefitted class should be viewed as an under-inclusive subset of the same industry, activity, or property), such that an exception is not applicable.

It should be noted that there may be overlap in the same industry, same activity, and same property exceptions because, in general, property is used in activities conducted by industries. The Joint Committee staff will look at the nature of the tax benefit being conferred in determining which of the exceptions might be applicable. Thus, as discussed below, the same industry exception will only apply to general tax benefits provided to an industry that is not defined by reference to particular activities in which an industry engages, or particular property in which an industry invests.

Provisions benefiting a "closed" class of taxpayers

In general, the Joint Committee staff believes that a revenue-losing provision that benefits 100 or fewer taxpayers does not qualify for the same industry, same activity, or same property exception if the class of taxpayers eligible for the provision is "closed." A class will be considered "closed" if other taxpayers engaging in the same transaction or activity, using the same type of property, or engaging in the same industry, within the same time period will not be able to benefit from the rule because the rule identifies eligible taxpayers in a manner that, on the face of the statute, is or will become impossible for others to meet. A class will not be considered closed for this purpose if all taxpayers (1) within an industry are entitled to the

benefit during a specified future period of time, or (2) engaging in a particular activity during a particular future period of time, are entitled to the same benefit. The key issue is whether, at a specific point in time, all taxpayers in an industry, engaging in an activity, or investing in property are entitled to similar benefits.

For example, if all of the taxpayers within an industry are entitled to pay corporate tax on their income at a 30-percent top marginal rate for taxable years beginning in 1997, the class of taxpayers entitled to the benefit will not be considered closed for purposes of the same industry exception because all of the taxpayers within the industry are entitled to the relief. On the other hand, if all of the taxpayers engaged in business within an industry as of January 1, 1997, are entitled to pay corporate tax on their income at a 30-percent top marginal rate for taxable years beginning in 1997, the class of taxpayers eligible for the relief would be considered closed because a new taxpayer entering an industry after January 1, 1997, and before December 31, 1997, would not be entitled to the relief.

b. Same industry exception

Application of same industry exception

The Joint Committee staff generally will interpret the same industry exception to apply only in the case of a general tax benefit that is provided to all taxpayers within an industry if the tax benefit is not determined by reference to the particular activities in which the taxpayers engage or the property in which the taxpayers invest.

The following are examples of the types of tax benefits that would qualify under the exception because they are general tax benefits provided to an entire industry:

(1) a lower top corporate tax rate applied to a specific industry;
(2) a deduction, credit, or exclusion provided to an industry that is not measured by reference to
    (a) any specific activity, or
    (b) the purchase or use of any specific property;
(3) the availability of an overall method of accounting (e.g., cash receipts and disbursements method) that is available to an entire industry; or
(4) an exception to an excise tax provided to an entire industry.

An example of a general tax benefit provided to all taxpayers within an industry would be a tax credit for all compensation expenses of the automobile manufacturing industry. The activity of compensating employees for services is sufficiently general in nature that it is not considered a separate activity that must be tested under the same activity exception described below; thus, such a tax credit could qualify for the same industry exception. On the other hand, a tax credit provided for expenses incurred for the retraining of auto workers would not be considered a general tax benefit because the credit to which a taxpayer is entitled is measured by reference to a specific activity.

Definition of industry

The term "industry" is not defined in the statute or legislative history of the Act. The Joint Committee staff believes that the determination of an "industry" generally should be made based on factors that demonstrate the degree of similarity of profit-making activities of a group of businesses. For purposes of this analysis, a single entity or corporate structure may be engaged in business in a number of different industries. In addition, the form of doing business or a particular corporate structure will not be determinative of the industry involved.

There is no provision in the Internal Revenue Code that provides definitive guidance as to how an industry should be defined. Therefore, the Joint Committee staff will consider the factors listed below in determining whether a class of benefitted taxpayers (although fewer than 100) nonetheless constitutes all members of the "same industry." No single factor will be controlling; the determination will be made based on the particular facts and circumstances of the provision at issue and the characteristics of the affected taxpayers. The existence of an industry is not determined by reference solely to the number of factors that may apply in a particular case.

The exception for "same industry" will apply if the same beneficial tax treatment is provided to all members of a group of businesses that can be viewed as a discrete industry on the basis of the following factors:

(1) whether the taxpayers compete within the same market(s);

(2) whether a prior governmental determination defines an industry (such as an antitrust case decided by a court);

(3) whether the taxpayers share common interests and concerns (as evidenced, for example, by a trade association or other industry group);

(4) whether the taxpayers are subject to the same type of governmental regulatory or licensing requirements;

(5) whether the taxpayers have common characteristics with respect to their production processes or the products or services produced that distinguish the group from other taxpayers;

(6) whether employees of the taxpayers are represented by a separate organization (e.g., a separate union);

(7) whether business activities are reported as an industry segment in conformity with Form 10-K or Form 20-F, in accordance with FAS 14 (Financial Reporting for Segments of a Business Enterprise);

(8) whether the taxpayers are engaged in a segment of the economy that commonly is reported for statistical purposes as a separate industry (e.g., for purposes of Commerce Department reports, reporting under the Census of Manufacturers, or reporting under the Standard Industrial Classification (SIC) or the North American Industry Classification System (NAICS)); and

(9) such other factor(s) as may be relevant to identifying a discrete or separate industry.

For example, the manufacture of passenger automobiles is a distinct industry. The taxpayers within the industry compete for the same customers (i.e., purchasers of automobiles), there are common characteristics of the production process that distinguish the manufacture of automobiles from the manufacture of other types of goods, the employees of the industry are represented by a separate union (e.g., United Auto Workers), and the taxpayers within the industry share common interests and concerns and are subject to the same regulatory requirements.

c. Same activity exception

In general

A revenue-losing provision granting a special tax benefit will not be subject to the line item veto if the same benefit is provided to all taxpayers who engage in the "same activity." The same activity exception may apply to tax benefits provided to for-profit business activities, as well as activities engaged in by similarly situated individuals and nonbusiness entities (e.g., tax-exempt organizations).

A critical issue is whether, as stated in the Statement of Managers for the Act, "the benefit is provided as an incentive to anyone who chooses to engage in the activity rather than to a closed group of specific taxpayers."[54] If the tax benefit is provided to only a "closed group" of taxpayers then the Joint Committee staff will conclude that the "same activity" exception has *not* been satisfied.

Whether or not a benefit is provided to a "closed group" does not end the inquiry. While a benefit that is determined to benefit a closed group would fail the same activity test, the fact that the beneficiaries of a provision do *not* constitute a closed group does not necessarily mean that the same activity exception will be satisfied.

Definition of same activity

The Joint Committee staff will consider the following factors in defining the term "activity" for purposes of the same activity exception: (1) the manner in which the activity is

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[54] House Report 104-191, page 38.

conducted (i.e., the processes by which an activity is conducted, rather than the end product of the activity, is the determining factor); (2) the uniqueness of the activity described; (3) the types of property or skills needed to conduct the activity; and (4) such other factors as may be relevant in a particular case. No single factor is controlling for purposes of this analysis. A tax benefit will not meet the same activity test if it is conditioned on a status (e.g., nature of the taxpayer taking the actions, particular geographic site where actions must be taken, etc.) that is unrelated to the actions for which the tax benefit is conferred.

For example, a tax benefit granted to employers operating hotels where meals are provided to employees on hotel premises would not qualify for the same activity exception because the "same activity" is providing meals to employees on the employer's premises and not all employers providing on-premises meals to their employees are receiving consistent treatment. The process of providing on-premises meals to employees on hotel premises is not sufficiently distinct from the process of providing on-premises meals to other employees at their worksite generally to be considered a separate activity.

If several industries engage in an activity for which a tax benefit is conferred, it is more likely that the special tax treatment for that activity will be deemed to satisfy the "same activity" exception. However, if an activity in which only the taxpayers within a single industry engage were provided special tax treatment, then such a tax-benefitted activity will be treated as an activity distinguishable from activities engaged in by other industries only if the tax-benefitted activity, considered by itself, is unique. For example, the activity of operating a nuclear power plant (even though engaged in by only the utility industry) is unique from all other activities conducted both within and without the utility industry, and, thus, could qualify for the "same activity" exception. Similarly, a tax credit for costs incurred in drilling oil and gas wells would qualify for the exception if all taxpayers in the oil and gas industry who engaged in the activity were entitled to the credit. The "same activity" exception would be satisfied, even though only taxpayers in the oil and gas industry would be expected to incur costs for drilling oil and gas wells.

If an activity receiving special tax treatment is conducted by taxpayers in several different industries, the "same activity" exception may be satisfied only if all taxpayers across all industries who engage in the activity are entitled to the special tax treatment. For example, incurring advertising expenses is not an activity that is unique to a single industry. Therefore, a benefit that is provided with respect to advertising expenses of a single industry would not qualify under the "same activity" exception.[55]

In general, the broader the activity for which a tax benefit is provided, the more likely that it is an "activity" for purposes of the "same activity" exception. However, a narrowly

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[55] Moreover, the same industry exception would not be satisfied because the tax benefit would be based on a specific activity, rather than being a general tax benefit for the particular industry. See the discussion in b., above.

described type of activity can meet the "same activity" exception if the activity (whether conducted within one industry or across several industries) is unique. Again, the focus for determining uniqueness will be upon the processes, operations, and conduct involved, rather than the characteristics of the end-product produced. For example, the end product (i.e., electricity) of a nuclear power plant is the same as the end product of other types of power plants, but the processes, operations, and conduct involved in operating a nuclear power plant are distinctly different from such processes, etc., of other types of power plants.

For example, the Statement of Managers indicates that providing special tax treatment for all persons who engage in research and development activities could satisfy the same activity exception. In this case, the activity for which a benefit is provided (i.e., research and development) is broadly defined and the benefit is provided to all taxpayers engaged in such activity. As another example, the Statement of Managers refers to the "activity" of drug testing. In contrast, the present-law orphan drug credit is available to all taxpayers who engage in the clinical testing of orphan drugs, but the process of clinically testing orphan drugs is not sufficiently distinct from the process of testing other drugs to constitute a separate activity for purposes of the same activity exception. The testing process for orphan drugs is governed by the same regulatory requirements, and generally involves the same scientific techniques, as the testing of other drugs. The primary differences between orphan drugs and other drugs instead relate to the different therapeutic effects of the drugs and the sales and marketing process because there is a more limited market for orphan drugs. Thus, the testing of orphan drugs is not a distinct activity from the activity of testing drugs generally and cannot be characterized as an activity for purposes of the same activity exception.

A tax benefit defined by reference to activity conducted within or without the United States will not be considered to fail the same activity exception. U.S. tax laws often make distinctions in the tax treatment of U.S. taxpayers based upon whether activities are conducted within or without the United States. For example, research eligible for the present-law research tax credit is limited to activities conducted within the United States. An extension of this credit would not be considered an activity limited by reference to a particular geographic site because it applies equally to everyone who conducts business in the United States. However, a tax benefit conferred for activities conducted only in certain areas in the United States, such as a particular city or in designated empowerment zones, or conducted only in a possession of the United States, generally would be considered a tax benefit that is not provided to all taxpayers engaging in the activity.[56]

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[56] If a tax benefit were granted for an activity but only when conducted at a narrow geographic site such that it is impossible for more than one taxpayer to engage in the activity at that site (e.g., building a football stadium on a specific site or constructing a bridge between 2 specified points), then the tax benefit *per se* would fail the same activity exception because the benefit would be provided to a "closed" group.

d. Same property and same investment exception

In general

The same property exception applies to a benefit provided with respect to the ownership of property if granted to all taxpayers who own such property. The same investment exception applies to a benefit provided with respect to all persons issuing the same type of investments.

As with the same activity exception, the fact that the benefit provided is available only to a "closed" class of taxpayers or a "closed" class of property will be a critical factor in determining whether the same property or same investment exception is available. In other words, the same property exception will not be satisfied if it is impossible for other taxpayers to either (1) own or (2) manufacture the type of property for which the tax benefit is conferred.

The legislative history of the Act refers to a tax credit provided for the purchase of a highly specialized type of computer and says that such a tax credit might qualify for the same property exception. If, however, this tax-preferred property were defined as a specific model of a supercomputer made by a particular manufacturer (or one made pursuant to a particular patent or containing a particular patented component), then the benefit would not be available to all taxpayers owning the same type of property, even though a theoretically unlimited number of taxpayers could purchase such specialized equipment. However, if a tax credit were provided for purchases of any supercomputers made by any manufacturer, all taxpayers owning the same type of property would be entitled to the same benefit. Thus, in order for the "same property" exception to apply, the class of property eligible for the tax benefit cannot be defined by reference to a specified manufacturer or specific model. Under this type of analysis, the same property exception would not be satisfied if a tax benefit were provided to only purchasers of a specified model of automobile (assuming there are fewer than 100 purchasers of such automobiles in a year).[57]

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[57] Note that this interpretation avoids the concern suggested in the floor statement of Senate Byrd with respect to a hypothetical tax benefit for purchasers of Rolls Royce automobiles. See, Congressional Record, March 27, 1996, S2961.

A different analysis arises if there are more than 100 purchasers of a specified model of automobile each year because the Joint Committee staff will consider statutory incidence as the test for determining whether the there are more than 100 beneficiaries. See the discussion in Part B., above. Thus, even though the property eligible for the benefit is a closed class (i.e., only vehicles made by one manufacturer), because there are more than 100 persons who will be able to claim the proposed tax credit for purchasing such a vehicle, the general definition of a "limited tax benefit" is not satisfied. On the other hand, if the general definition is satisfied (i.e., the statutory incidence of the proposed tax benefit will fall on fewer than 100 beneficiaries in a given year), then the issue of "open" versus "closed" class will be relevant to the determination of whether the exceptions for "same activity" or "same property" are satisfied.

If special tax treatment were provided for the purchase of a class of automobile that could be manufactured by any firm, the question would follow whether substitutable products are denied the favorable tax treatment -- is the tax-preferred class of automobiles sufficiently distinct from other automobiles (in the sense that a supercomputer is distinct from a personal computer)?

Definition of same property

The Joint Committee staff will consider the following factors in defining property for purposes of the same property exception: (1) the use of the property (i.e., whether there is competition with other products for the same or similar use); (2) the defining characteristics of the property; (3) the useful life of the property as compared to other types of similar property; (4) the substitutability of other property to perform the same function; and (5) such other factors as may be relevant in a particular case. As with the same industry and same activity exceptions, no single factor is controlling. The determination of property for purposes of the same property exception will be based on the level of technology in effect at the time a provision is adopted.

For example, the use and defining characteristics of electric typewriters are sufficiently similar to the use and characteristics of manual typewriters that both should be considered the same property and a tax benefit provided solely with respect to electric typewriters would not qualify under the same property exception. Similarly, a tax benefit provided for the ownership of a specific type of word processing software but not another type of word processing software would not qualify under the same property exception if other word processing software is sufficiently similar to be treated as the same property.

If the use of property crosses several industries or activities, then a tax benefit provided with respect to the property is more likely to satisfy the same property exception. However, if a tax benefit is provided with respect to property used only by the taxpayers within a single industry, then such tax-preferred property only will be considered distinguishable from property used by other industries if the use and characteristics of the property are unique.[58]

If property receiving special tax treatment is owned by taxpayers in several different industries, the "same property" exception may be satisfied only if all taxpayers across all industries who own the property are entitled to the special tax treatment. For example, the provision of a special tax benefit for the use of word processing equipment by the automobile manufacturing industry would not qualify under the same property exception because the use of such word processing equipment is not unique to the process of manufacturing automobiles and no other industry.

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[58] The Statement of Managers provides an example of a provision that "sets forth depreciation treatment for equipment that is *used only* [emphasis added] by automobile manufacturers." Such a provision could qualify under the same property exception even though the benefit is provided only to taxpayers within a single industry.

Definition of same investment

For purposes of defining whether all taxpayers issuing a type of investment are receiving the same treatment, the key factors in determining what constitutes the same type of investment will be (1) the specific characteristics of the specific type of investment, (2) the substitutability of other types of investments, and (3) such other factors as may be relevant given the type of tax benefit being conferred. For example, the legislative history of the Act provides that a provision that affects the deductibility of interest with respect to certain types of debt instruments would not be a limited tax benefit, as long as any person who issued that type of debt instrument receives the same treatment.

As with the same activity and same property exceptions, the same investment exception will not be satisfied if a tax benefit is conferred on a "closed group" of taxpayers issuing an investment (e.g., if preferential treatment were limited to taxpayers who had issued a type of investment on a past date).

In addition, the more broadly the tax-preferred investment is defined, the more likely that a tax benefit provided to the issuers of the investment will qualify for the same type of investment exception.

e. Exceptions for special treatment based solely on business size or form, general demographic conditions of individuals, amount involved, or generally available election

The Act further provides that, even if a revenue-losing provision would benefit 100 or fewer beneficiaries during a given year, such provision will not be deemed to be a "limited tax benefit" if any difference in the treatment of persons is based solely on (1) in the case of businesses and associations, the size or form of the business or association involved, (2) in the case of individuals, general demographic conditions, such as income, marital status, number of dependents, or tax return filing status, (3) the amount involved, or (4) a generally available election under the Internal Revenue Code of 1986.[59] The Statement of Managers indicates that, as with the exceptions for "same industry," "same activity," and "same property," these exceptions provided for in section 1026(9)(B) of the Act were intended to allow special tax treatment granted to similarly situated taxpayers on the basis of their size or legal or demographic characteristics (as opposed to on the basis of the particular activities engaged in by the taxpayer) to escape characterization as a "limited tax benefit." The Statement of Managers gives as examples meeting the statutory exceptions a provision that grants preferential treatment for small businesses, a cap based on the dollar amount of a taxpayer's investment or the number of units produced by a taxpayer, and a case where fewer than 100 taxpayers are expected to choose one of the alternative treatments that may be elected under the Code.

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[59] Section 1026(9)(B)(iii) of the Budget Act.

The Joint Committee staff will construe the statutory exceptions based on size or form of business entity, or amount involved, so that the exceptions are not satisfied if a proposed statutory classification creates a "closed" group of benefited taxpayers (e.g., taxpayers eligible for the special treatment are defined by reference to one specific dollar amount of assets or receipts as measured on one particular date). In contrast, the use of dollar (or other numeric) caps or floors that serve as proxies to distinguish small from large entities or transactions rather than to limit the benefit to a fixed group of taxpayers generally will be viewed as satisfying the statutory exceptions. This interpretation is needed to prevent the exceptions from eliminating the concept of limited tax benefits.

The concept of "general" demographic conditions suggests that descriptions of narrow, specific characteristics of particular individuals (or attempts to single out particular individuals by reference to an event--e.g., birth or death--involving that individual occurring on one particular date or at one specific site) will not satisfy the exception for general demographic conditions. Because most tax benefits conferred in general terms are likely to benefit well over 100 taxpayers, it is expected that the general demographic exception will have very limited applicability. One example of a provision that would qualify for the exception would be a provision to exempt from the individual income tax (or to provide a higher personal exemption amount to) any person over the age of 120. The sole determining factor for eligibility for the tax benefit is the taxpayer's age and there are likely to be 100 or fewer beneficiaries in each fiscal year in which the provision is in effect. However, because age is a general demographic condition, the exception would apply.

D. Transitional Relief for 10 or Fewer Beneficiaries

1. In general

A limited tax benefit includes any Federal tax provision that provides temporary or permanent transitional relief for 10 or fewer beneficiaries in any fiscal year from a change to the Internal Revenue Code of 1986. There are two exceptions. First, transitional relief is not a limited tax benefit to the extent it provides for the retention of prior law for all binding contracts (or other legally enforceable obligations) in existence on a date contemporaneous with Congressional action specifying such a date. Second, transitional relief is not a limited tax benefit if it is a technical correction to previously enacted legislation that is estimated to have no revenue effect.

The limited tax benefit definitions with respect to transitional rules differ from those governing revenue-losing provisions in two principal respects. First, the threshold number of beneficiaries necessary to avoid limited tax benefit classification is lower for transitional relief than for a revenue-losing provision. Transitional relief cannot be a limited tax benefit if it benefits more than 10 beneficiaries; while a revenue-losing provision can be a limited tax benefit unless it benefits more than 100 beneficiaries.

Second, a revenue-losing provision is not a limited tax benefit, even if it affects a small number of beneficiaries (such as 10 or fewer) if the provision falls within certain categories, generally such that all persons in the same industry, engaged in the same activity, owning the same type of property, or issuing the same type of investment receive the same treatment. There also are exceptions for treatment that differs as a result of size, demographic conditions, amounts involved, or a general election provided under the Code. The statute does not provide any such exceptions in the case of transitional relief.

A number of issues are expected to arise because the line item veto legislation distinguishes "transitional relief" from other situations that may appear to involve a relative benefit for a small group of taxpayers. It is necessary to determine when an exception from a change in law that benefits a small group of taxpayers should be considered "transitional relief" as opposed to part of the basic scope and structure of the new law. This determination may be particularly difficult in situations that might be deemed to involve permanent transitional relief. Also, it is necessary to determine how to treat certain provisions that may provide special rules for a particular class of taxpayers in the context of a general change in law, and thus may provide a relative benefit even though, compared to prior law, they may be revenue-losing or revenue-raising provisions.

Another set of issues relates to the exceptions from the definition of limited tax benefit. Transitional relief is not a limited tax benefit if it retains prior law for binding contracts or other legally enforceable obligations in existence on a date contemporaneous with Congressional action specifying such date. Questions may arise regarding the extent to which the statute itself can presume something to be a legally enforceable obligation, the nature of Congressional action, and the determination whether a date is "contemporaneous" with such action.

Transitional relief also is not a limited tax benefit if it is a technical correction to previously enacted legislation that is estimated to have no revenue effect. Under this standard, the nature of the revenue estimate for the particular provision can determine whether the provision is a limited tax benefit.

2. Specific issues and examples

a. Definition of "transitional relief"

Taxpayers affected--"closed" class

The Act does not define "transitional relief." However, the conference report states the following regarding transition rules:

> This provision covering transition rules is intended to address the type of special rules used extensively in prior tax legislation. For example, in the Tax Reform Act of 1986 (the "1986 Act"), which included a number of revenue raising tax provisions, various specifically identified taxpayers were provided special rules that

> exempted them from treatment under the general revenue raising provisions. One provision in the 1986 Act changed the rules for how multinational corporations could allocate interest expenses for foreign tax credit purposes. The provision included a favorable rule for banks, and also included a special exception allowing "certain" non-banks to use the favorable bank rule. The special exception applied to any corporation if "(A) such corporation is a Delaware corporation incorporated on August 20, 1959, and (B) such corporation was primarily engaged in the financing of dealer inventory or consumer purchases on May 29, 1985 , and at all times thereafter before the close of the taxable year" Public Law 99-514, 100 Stat. 2548, sec. 1215(c)(5). If 10 of fewer taxpayers were expected to benefit from the special exception, this provision would constitute a limited tax benefit under the conference agreement definition, and would be subject to the President's cancellation authority.[60]

Based upon the type of example given in the legislative history regarding transitional relief, as well as the concern expressed elsewhere in the legislative history regarding benefits for a "closed" group of taxpayers,[61] the Joint Committee staff will treat a provision as transitional relief if it refers to a "closed" class of taxpayers. For this purpose, a class will be considered "closed" if other taxpayers engaging in the same transaction or activity, or using the same type of property or engaging in the same industry, in the same time period, will not be able to benefit from the rule because the rule identifies eligible taxpayers in a manner that is or will become impossible for others to meet. If a provision is expected as a practical matter to benefit a fixed class of taxpayers, the Joint Committee staff will also consider this to be a factor. In other limited circumstances, factors other than the existence of a closed class may also indicate that a provision is transitional relief.

Examples of transitional relief include (without limitation) a rule granting relief from a change in law to taxpayers incorporated on a certain date, or permitting favorable ongoing treatment to taxpayers engaging in a certain type of business activity or business structure before a certain date. If such a provision is estimated to benefit 10 or fewer taxpayers in any fiscal year, and does not qualify for the contemporaneous binding contract (or other legally enforceable obligation) or technical corrections exceptions for transitional relief, it will be a limited tax benefit.

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[60] H.R. Rept. 104-491. 104th Cong, 2d Sess. (March 21, 1996), p.39.

[61] See discussion, supra, regarding "closed" groups of taxpayers in the context of revenue-losing provisions.

Relief that may differ from prior law

In some instances, legislation may change the law generally, and also may provide that a closed class of taxpayers experiences a different, apparently more favorable change that does not precisely retain prior law. The more favorable change for the particular class might independently be considered either a revenue-losing or revenue-raising provision if compared to prior law. The question arises how such changes in the context of a general change to prior law should be treated for purposes of applying the limited tax benefit rules.

Revenue-losing provisions

If the benefit provided to a closed class of taxpayers in connection with a more general change in the law is a revenue-losing provision, the Joint Committee staff will analyze the provision under the rules applicable to revenue-losing provisions as well as under the rules applicable to transitional relief. If the provision would be a limited tax benefit under either set of rules, it will be identified as a limited tax benefit.

For example, assume that a change in law increases all tax rates by 15 percent for all taxpayers for all taxable years after a certain date, except for those taxpayers engaging in a certain specified transaction under a binding contract or legally enforceable obligation in effect on a date contemporaneous with Congressional action specifying such a date, who will receive a 2-percent reduction in tax (estimated as a revenue-losing reduction) with respect to gain from that transaction. It is expected that a group of 10 or fewer taxpayers will benefit from the reduction. Because the provision is a revenue-losing provision, and because it benefits fewer than 100 taxpayers, it will be analyzed to determine whether any of the exceptions under the revenue-losing limited tax benefit rules (for taxpayers in the same industry, activity, or otherwise similarly situated) will apply. Since the provision applies to a "closed" class of taxpayers, the exceptions applicable to revenue-losing provisions for taxpayers engaging in the same activity or owning the same type of property will not apply under the Joint Committee staff application of those exceptions;[62] thus, the provision is a limited tax benefit when analyzed under the rules applicable to revenue-losing provisions.

In the above example, even if the provision were found not to be a limited tax benefit under the "revenue-losing provision" test, it also would be subject to the transitional rule test. Under this test, the provision would be a limited tax benefit because it does not satisfy the requirements for the exception for binding contracts or legally enforceable obligations in existence on a date contemporaneous with Congressional action specifying such a date. That exception applies only if the relief retains prior law; while in the example, the relief provides a result more favorable than prior law.

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[62] See discussion at Part III.C.2., supra, regarding the effect of a "closed" class on the exceptions to limited tax benefit status for revenue-losing provisions expected to benefit 100 or fewer taxpayers.

In the above example, the revenue-losing provision is a limited tax benefit under both the revenue-losing rules and the transitional relief rules. However, if a revenue-losing provision that is also transitional relief is a limited tax benefit under either (but not both) of such rules, it will be identified as such.

Retention of all or a part of prior law

In some cases, transitional relief may retain a part, rather than all, of prior law, thus possibly raising revenue from the benefitted class of taxpayers. The Joint Committee staff will interpret transitional relief to include retention of all or a part of prior law.

For example, assume that legislation repeals special tax benefits for certain types of activities conducted after the date of enactment, but phases out the benefits more slowly for a particular closed class of taxpayers in existence on a particular date. The class is not limited by reference to binding contracts (or other legally enforceable obligations) in effect on a date contemporaneous with Congressional action specifying such a date. Although the phase-out may be a revenue-raising provision when compared to prior law, it applies to a closed class of taxpayers and it still retains a part of prior law, and thus is considered transitional relief. If 10 or fewer taxpayers are expected to benefit from the phase-out in any fiscal year, the phase-out will be a limited tax benefit (assuming it is not eligible for the technical correction exception).

As another example, assume that new legislation generally provides a 10-percent across the board increase in Federal income tax rates for all taxpayers. However, an exception is provided for one particular identified taxpayer, for whom the increase in the rate is only 1 percent. Assume that each of these rate increases is estimated to raise revenue compared to prior law. The special 1-percent rule would be considered transitional relief because it applies to a "closed" class of taxpayers, and would be a limited tax benefit because it is expected to benefit 10 or fewer taxpayers in a fiscal year (assuming it is not eligible for the technical correction exception).[63]

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[63] As in the case of revenue-losing provisions, the manner in which legislation is drafted may produce a situation in which striking a provision would produce a result different from subjecting the benefitted class to the general rule. In such a case, the provision would not be a limited tax benefit. For example, if a statute defined two separate and mutually exclusive classes of taxpayers, one of which received a rate increase of 15 percent, while the other (a closed class) received a rate increase of 1 percent, the provision affecting the closed class would not be a limited tax benefit unless striking the words relating to that provision would eliminate the exception (i.e., would subject the closed class to the general 15-percent rate increase). If striking the words had the effect of returning that closed class to prior law-- still a result better than the result for the general class of taxpayers-- the provision would not be a limited tax benefit subject to Presidential cancellation authority because no words could be stricken that would result in the closed class obtaining the same treatment as the general class of taxpayers. See Part III. A., supra.

b. Exception for transitional relief that retains prior law for binding contracts (or other legally enforceable obligations) in existence on a date contemporaneous with Congressional action specifying such a date

Definition of binding contract or other legally enforceable obligation

The mere fact that a statute or legislative history may state that for purposes of a certain provision, specified situations shall be deemed to create or not to create a binding contract or other legally enforceable obligation will not govern the determination whether in fact there is a binding contract or other legally enforceable obligation.

Whether a binding contract or other legally enforceable obligation exists is a question of State law. Taxpayers and the IRS must determine whether the relief is available based on all the facts and circumstances. The Joint Committee staff will not attempt to interpret or apply the terms generally, or in particular facts and circumstances. Thus, in applying the line item veto legislation, the Joint Committee staff will treat any language purporting to define what is a binding contract or legally enforceable obligation as beyond the scope of those terms.

For example, if statutory language provides relief to all binding contracts or other legally enforceable obligations in existence on the date contemporaneous with Congressional action specifying such date, and there are 10 or fewer taxpayers who would benefit from such relief, the provision is not a limited tax benefit. Suppose, however, the statutory language also provides that, for purposes of this transitional relief, an offer will be considered a binding contract. The additional language will be considered a separate provision and if it benefits 10 or fewer taxpayers, that provision will be a limited tax benefit. The remaining language granting relief to binding contracts or other legally enforceable obligations will not be a limited tax benefit.[64]

Situations other than legally enforceable obligations

In many past instances, transitional relief has been provided not only for binding contracts but also if taxpayers have taken certain steps recognized as showing a good faith intent to go forward and possibly involving significant expense, or causing a business expectation to others that the transaction will go forward. For example, transitional relief has sometimes been

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[64] Suppose that the statutory language had not provided any relief for binding contracts or other legally enforceable obligations, but only for offers. Suppose further that only five taxpayers have offers outstanding, while five others had their offers accepted (i.e., those taxpayers have executed binding contracts). In such a case, the offer rule would still be a limited tax benefit in its entirety. If it became the subject of a veto, the taxpayers with binding contracts would not be protected because the statute had not provided any relief specifically for binding contracts or other legally enforceable obligations. The statute cannot be rewritten through the exercise of a veto, other than to strike the limited tax benefit language. See Part III. A., supra.

granted from a provision changing the tax treatment of the buyer or of the seller of stock with a general effective date for all sales after a specified date, in the case of sales pursuant to a tender offer outstanding on the date of Congressional action. Another example is the provision of transitional relief for certain transactions for which there has been a specified type of filing with the SEC by the specified date.

Because such relief is not by its terms limited to legally enforceable obligations, it would be identified as a limited tax benefit if 10 or fewer taxpayers were expected to benefit from the provision in any fiscal year.

Definition of "Congressional action"

Transitional relief is not a limited tax benefit to the extent it retains prior law for all binding contracts or other legally enforceable obligations in existence on a date contemporaneous with Congressional action specifying such a date.

Neither the statute nor legislative history defines the term "Congressional action" for this purpose. The Joint Committee staff will consider examples of Congressional action to include, for example, the introduction of a bill by any member of Congress; the release of a Chairman's mark; the release of a joint statement by the Chairman of the House Ways and Means and Senate Finance Committees; or a date of conference action.

Thus, as one example, if an introduced bill contains an effective date providing transitional relief for binding contracts or other legally enforceable obligations contemporaneous with the date of introduction of the bill, the exception will be satisfied. Even if 10 or fewer taxpayers are expected to benefit from the transitional relief, the provision of such relief will not be identified as a limited tax benefit if the bill goes to conference retaining the original effective date. At the same time, if the bill were modified at any date of later Congressional action (including a date of conference action) to adopt a contemporaneous date with respect to binding contracts (or other legally enforceable obligations) in existence on such date, that new date similarly would not cause identification as a limited tax benefit.

Definition of "contemporaneous"

Questions may arise as to how close in time to the relevant Congressional action a specified date must be in order to qualify for the binding contract exception to transition limited tax benefits. The Joint Committee staff will interpret the term "contemporaneous" to mean a date that is the same as the date of the relevant Congressional action.

As one example of a date that would not satisfy the requirements for the exception, transitional relief for binding contracts (or other legally enforceable obligations) entered into before a date that is six months before the relevant Congressional action generally will not be considered a "contemporaneous" date. The fact that the date might have been selected as the time of the first announced transaction calling attention to the operation of present law, or as the

date the Internal Revenue Service first announced that it would challenge a particular tax result, would not cause the date to be considered "contemporaneous" for purposes of the limited tax benefit rule. Thus, if such transitional relief benefits 10 or fewer taxpayers and is not excepted as a technical correction, it will be identified as a limited tax benefit. By contrast, transitional relief for contracts in existence as of the date of relevant Congressional action will not be a limited tax benefit, even though possibly the same 10 or fewer taxpayers might be the beneficiaries of the transitional relief.

Similarly, transitional relief for binding contracts or other legally enforceable obligations entered into as of a date six months following the date of relevant Congressional action also would not satisfy the "contemporaneous" requirement. Again, if it were determined that 10 or fewer taxpayers would be expected to benefit in any fiscal year, the transition rule would be a limited tax benefit.

A common form of effective date is one providing that legislation has a generally prospective effective date (e.g., for transactions or for taxable years after a date in the future), but retains present law for transactions occurring pursuant to a legally enforceable obligation in existence as of a date of Congressional action specifying such date. Taxpayers who complete their transactions before the general effective date also would be able to treat their transactions under the present law rules, but this language generally does not constitute a limited tax benefit, even if only 10 or fewer taxpayers (without binding contracts or other legally enforceable obligations) were expected to be able to complete their transactions before the general effective date. Any other interpretation would require the addition of a substitute general effective date (e.g., the date of Congressional action chosen for the binding contract transition) rather than the mere striking of language by a veto.[65]

Requirement that the provision retain prior law

The exception to limited tax benefit treatment only applies if the provision "retains prior law" for the relevant binding contracts (or other legally enforceable obligations). As described above, the Joint Committee staff will treat a provision as transitional relief if it retains all or a part of prior law. Similarly, the binding contract (or other legally enforceable obligation) exception will apply to any such transition.

For example, if a provision repeals a tax benefit for a certain type of activity and phases out the repeal more slowly only for taxpayers with a binding contract (or other legally enforceable obligation) in existence on a date contemporaneous with Congressional action

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[65] As in the case of revenue-losing provisions, if there is no specific statutory language that provides the benefit to a class of taxpayers and that can be stricken from the statute in the form of a veto, there is not a limited tax benefit under the Act. See Part III. A., supra.

specifying such a date, the phase-out rule will not be a limited tax benefit even if 10 or fewer taxpayers are expected to benefit from the phase out.

c. Exception for a technical correction to prior law that is estimated to have no revenue effect

Transitional relief benefitting 10 or fewer taxpayers is not a limited tax benefit if it is a technical correction to previously enacted legislation that is estimated to have no revenue effect.

There have been instances in the past in which technical correction legislation has been estimated to have a revenue effect. If there is any estimated revenue effect to a technical correction that is itself a transitional relief provision and is expected to benefit 10 or fewer taxpayers, the provision will not qualify for the technical correction exception from identification as a limited tax benefit.

However, suppose a technical correction adverse to taxpayers is adopted with transitional relief for transactions occurring pursuant to binding contracts (or other legally enforceable obligations) as of a date contemporaneous with the Congressional action specifying the technical correction. Even if such a technical correction were estimated to have a revenue effect, the transitional relief provision of the technical correction satisfies the requirement for binding contracts or other legally enforceable obligations in existence on a date contemporaneous with the date of Congressional action specifying such a date. Thus, the transitional relief provision of the technical correction is not a limited tax benefit.

IV. EXAMPLES OF APPLICATION OF LINE ITEM VETO TO LIMITED TAX BENEFITS

A. Examples of Revenue-Losing Provisions

1. Extension of the orphan drug tax credit (sec. 1205 of the Small Business Job Protection Act of 1996 (the "Small Business Act"))

Prior to January 1, 1995, a 50-percent tax credit was allowed for qualified clinical testing expenses incurred in the testing of certain drugs for rare diseases or conditions. The Small Business Act extended the credit from July 1, 1996, through May 31, 1997.

If the Act had been in effect, this provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit fewer than 100 drug companies in at least one fiscal year in which the provision would be in effect, and all persons engaged in the activity of drug testing are not treated the same. Only certain types of drug testing qualify for the credit.

2. Extension of binding contract date for biomass and coal facilities (sec. 1207 of the Small Business Act)

Under a tax credit is provided for fuel produced from certain "nonconventional sources." Under prior law, in the case of synthetic fuel produced from coal and gas produced from biomass, the credit was available only for fuel from facilities placed in service before January 1, 1997, pursuant to a binding contract entered into before January 1, 1996. The Small Business Act extended the credit to facilities placed in service before July 1, 1998, pursuant to a binding contract entered into before January 1, 1997.

If the Act had been in effect, the Small Business Act provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit 100 or fewer beneficiaries, and an exception would not have been available. The separate industry exception would not have been available because the tax benefit does not apply to all persons within a single industry. Even if the production of fuel from nonconventional sources were a separate industry, the industry exception would not have applied because the benefit is provided to a closed class of taxpayers. Similarly, the separate activity exception would not have been available because the benefit is provided to a closed group of taxpayers--only those persons producing fuel from nonconventional sources in facilities placed in service before July 1, 1998.

3. Exemption from diesel fuel dyeing requirements with respect to certain States (sec. 1801 of the Small Business Act)

Under present law, an excise tax is imposed on diesel fuel removed from a terminal facility unless the fuel was destined for a nontaxable use and is indelibly dyed pursuant to Treasury Department regulations. A similar dyeing regime exists for diesel fuel under the Clean

Air Act, but the State of Alaska is partially exempt from the dyeing regime of the Clean Air Act. The Small Business Act exempted diesel fuel sold in the State of Alaska from the excise tax dyeing requirement during the period when that State is exempt from the Clean Air Act dyeing requirement.

If the Act had been in effect, the Small Business Act provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit 100 or fewer beneficiaries in at least one fiscal year in which the provision would be in effect, and it would not fall within any of the stated exceptions. The industry exception would not have been available because the benefit is not provided to an entire industry. The provision does not treat all persons engaged in the same activity the same way, because the provision applies only to those taxpayers performing the activity in a particular geographic locale.

4. Modification to excise tax on ozone-depleting chemicals (sec. 1803 of the Small Business Act)

Under present, an excise tax is imposed on the sale or use by the manufacturer or importer of certain ozone-depleting chemicals. Taxable chemicals that are recovered and recycled within the United States are exempt from tax. The Small Business Act extended the exemption to imported recycled halons.

If the Act had been in effect, the Small Business Act provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit 100 or fewer importers in at least one fiscal year in which the provision would be in effect, and it would not fall within any of the stated exceptions. The provision does not provide similar treatment to all similarly situated taxpayers.

5. Tax-exempt bonds for sale of Alaska Power Administration Facility (sec. 1804 of the Small Business Act)

Under present law, tax-exempt bonds may be issued for the benefit of certain private electric utilities. If the bonds are used to finance acquisition of existing property by these utilities, a minimum amount of rehabilitation must be performed on the property as a condition of receiving the tax-exempt bond financing. The Small Business Act waived the rehabilitation requirement in the case of bonds to be issued as part of the sale of the Snettisham facility by the Alaska Power Administration.

If the Act had been in effect, the Small Business Act provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit only one issuer of tax-exempt bonds, and it would not fall within any of the stated exceptions. The provision does not provide a benefit to an entire industry. The same activity exception would not be satisfied because the benefit is provided to a closed class--no other issuers of tax-exempt bonds would benefit from the provision.

6. Organizations subject to section 833 (sec. 351 of the Health Insurance Portability and Accountability Act of 1996)

Prior-law section 833 (created in the Tax Reform Act of 1986) provides special tax benefits to Blue Cross or Blue Shield organizations existing on August 16, 1986, which have not experienced a material change in structure or operations since that date. The Health Insurance Portability and Accountability Act of 1996 extended this special rule to other similarly-structured organizations that were in existence on August 16, 1986, and have not materially changed in structure or operations since that date.

Had the Act been in effect, the provision in the Health Insurance Portability and Accountability Act would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit fewer than 100 beneficiaries, and it would not fall within any of the stated exceptions. The provision does not provide a benefit to an entire industry. The same activity exception would not apply because the benefit would be available only to a closed group of taxpayers that were in existence in 1986, and would not be available to any newly formed entities. In addition, the provision does not make the treatment of the class of taxpayers under the provision equivalent to the treatment of all other similarly situated taxpayers.

7. Exemption from the generation-skipping transfer tax for transfers to individuals with deceased parents (sec. 11074 of the Balanced Budget Act of 1995 (the "BBA")[66])

Under present law, a generation-skipping transfer tax generally is imposed on transfers to an individual who is more than one generation younger than the transferor. An exception provides that a transfer from a grandparent to a grandchild is not subject to the generation-skipping tax if the grandchild's parent (who is the grandparent's child) is deceased at the time of the transfer. The BBA provision would have expanded the present-law exception to apply also in other limited circumstances, e.g., if the transferor has no living lineal descendants and makes a transfer to a grandniece or grandnephew whose parents are deceased.

If the Act had been in effect, the BBA provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit 100 or fewer beneficiaries in at least one fiscal year in which the provision would have been in effect, and it would not fall within any of the stated exceptions. It would not provide the same treatment to all persons engaged in the same activity--making generation-skipping transfers--because a transferor could only obtain the beneficial treatment if several factors were met: (1) the transferor has no lineal descendants; (2) the transferee is one of a limited class of relatives (in general, the transferee must be a descendant of the transferor's parents); and (3) the transferee's parent(s) must be deceased. There is no general demographic condition (or other distinguishing factor that meets

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[66] The Balanced Budget Act of 1995 (H.R. 2491, 104th Cong.) was vetoed by President Clinton.

the exceptions set forth in the Act) that constitutes the sole reason for persons engaged in the same activity being treated differently.

8. Common investment fund for private foundations (sec. 11276 of the BBA)

The BBA would have granted tax-exempt status to any cooperative service organization comprised solely of members that are tax-exempt private foundations and community foundations, if the organization met certain requirements and was organized and operated solely to hold, commingle, and collectively invest and reinvest funds contributed by the members in stocks and securities, and to collect income from such investments and turn over such income, less expenses, to the members.

If the Act had been in effect, the BBA provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit 100 or fewer beneficiaries in at least one fiscal year in which the provision would have been in effect (i.e., 100 or fewer entities would benefit from the tax-exempt status), and it would not fall within any of the stated exceptions. The provision would not have benefited an entire industry. The provision also would not have treated all persons engaged in the same activity the same way; mutual funds that are engaged in the same type of activity would not have received the benefit of the provision.

9. Modification to tax-exempt bond penalties for local furnishers of electricity and gas (sec. 11333 of the BBA)

Under present law, tax-exempt bonds may be issued to benefit private businesses engaged in the furnishing of electric energy or gas if the business's service area does not exceed either two contiguous counties or a city and one contiguous county. If, after such bonds are issued, the service area is expanded beyond the permitted geographic area, interest on the bonds becomes taxable and interest paid by the private parties on bond-financed loans becomes nondeductible. The BBA would have allowed private businesses engaged in the local furnishing of electricity or gas to expand their service areas beyond the geographic bounds allowed under present law without penalty under certain specified circumstances.

If the Act had been in effect, the BBA provision would have been a "limited tax benefit" because it was estimated to lose revenue, it was expected to benefit 100 or fewer beneficiaries in at least one fiscal year in which the provision would be in effect, and it would not fall within any of the stated exceptions. The provision would not have applied to an entire industry. The same activity exception would not have been available because all persons engaged in the activity of generating electricity or gas would not be treated the same. The process of producing electricity or gas locally is not different from the process of generating electricity or gas generally.

10. Special rule under section 2056A (sec. 11614 of the BBA)

Under present law, a marital deduction generally is allowed for estate and gift tax purposes for the value of property passing to a spouse. The marital deduction is not available for

property passing to a non-U.S.-citizen spouse outside a qualified domestic trust ("QDT"). The requirements for a qualified domestic trust were modified in the Omnibus Budget Reconciliation Act of 1990 ("OBRA 1990"). The BBA would have allowed trusts created before the enactment of OBRA 1990 to qualify as QDTs if they satisfy the requirements that were in effect before the enactment of OBRA 1990.

If the Act had been in effect, the BBA provision would have been a "limited tax benefit" because it was intended to lose revenue, it was expected to benefit 100 or fewer beneficiaries in at least one fiscal year in which the provision would have been in effect, and it would not fall within any of the stated exceptions. The provision would have benefited a closed group of taxpayers. Trusts created before the enactment of OBRA 1990 would have been treated differently than trusts created after the enactment of OBRA 1990.

11. Community development corporations (sec. 13311 of the Omnibus Budget Reconciliation Act of 1993 ("OBRA 1993")

OBRA 1993 included a provision that created an income tax credit for entities that make qualified cash contributions to one of 20 "community development corporations" ("CDCs") to be selected by the Secretary of HUD using certain selection criteria. Each selected CDC could designate which contributions (up to $2 million per CDC) would be eligible for the credit.

If the Act had been in effect, the OBRA 1993 provision would have constituted a "limited tax benefit". It was expected to provide a benefit to 100 or fewer contributors in at least one fiscal year in which the provision would be in effect. Assuming that making contributions to CDC's is a separate activity, all persons who engage in the activity of making contributions to CDCs were not treated the same (i.e., only those persons contributing to the selected CDC's receive the benefits).

B. Examples of Provisions that Provide Temporary or Permanent Transitional Relief

1. Temporary exemption from the original income tax for the sitting President

The 1913 law that imposed the first income tax provided an exemption for the sitting President of the United States for the remainder of his term. If the Act had been applicable at the time, the provision exempting the sitting President's income from tax would have been a limited tax benefit because it provided transition relief to a single taxpayer (i.e., a closed class) and the binding contract or other legally enforceable obligation exception would not apply.

2. Transition relief from repeal of section 936 credit (sec. 1601 of the Small Business Act)

Certain domestic corporations with business operations in the U.S. possessions may elect the section 936 credit, which significantly reduces the U.S. tax on certain income related to their operations in the possessions. The Small Business Act repealed section 936 for taxable years beginning after December 31, 1995. However, transition rules were provided under which

corporations that were existing claimant under section 936 were eligible to claim credits for a transition period. One of these transition rules applied to a corporation that is an existing claimant with respect to operations in Guam, American Samoa, or the Commonwealth of the Northern Mariana Islands to continue to determine its section 936 credit with respect to its operations in such possessions under prior law for its taxable years beginning before January 1, 2006.

If the Act had been in effect, the transition rule for corporations operating in Guam, American Samoa, or the Commonwealth of the Northern Mariana Islands would have been a limited tax benefit because it was expected to provide transitional relief to 10 or fewer beneficiaries (it benefits a closed class of taxpayers, those who were existing 936 claimants), and it would not have met the binding contract exception.

3. Financial institution transition rule to interest allocation rules (sec. 1215(c)(5) of the Tax Reform Act of 1986 (the "1986 Act"))

A provision in the 1986 Act changed the rules relating to how multinational corporations allocate interest expense for foreign tax credit purposes. The provision included a favorable rule for banks, and also included a special exception allowing "certain" nonbanks to use the favorable bank rule. The special exception applied to any corporation if "(A) such corporation is a Delaware corporation incorporated on August 20, 1959, and (B) such corporation was primarily engaged in the financing of dealer inventory or consumer purchases on May 29, 1985, and at all times thereafter before the close of the taxable year."

Had the Act been in effect, this transition rule would have been a "limited tax benefit" if it had been estimated to provide transitional relief to 10 or fewer beneficiaries in at least one fiscal year in which the provision would be in effect.

4. Transition relief from private activity bond requirements (sec. 10631(c)(3) of the Omnibus Budget Reconciliation Act of 1987 ("OBRA 1993"))

Private activity bonds are generally subject to a State's annual private activity volume limitation. OBRA 1993 created a new category of private activity bond for bonds issued by a governmental unit to acquire certain nongovernmental output property, e.g., electrical generation facilities, thereby subjecting such bonds to the private activity volume limitation. However, prior law was retained for "bonds issued--(A) after October 13, 1987, by an authority created by a statute--(i) approved by the State Governor on July 24, 1986 and (ii) sections 1 through 10 of which became effective on January 15, 1987, and (B) to provide facilities serving the area specified in such statute on the date of its enactment." Thus, such bonds were not subjected to the private activity volume limitation.

Had the Act been in effect, the provision retaining prior law for certain bonds would have been a "limited tax benefit" because it provided transition relief to a closed class; no other issuers of tax-exempt bonds would benefit from the provision.

5. Transition rule with respect to modifications to deductions for dividends paid on employer securities (sec. 7301(f) of the Omnibus Budget Reconciliation Act of 1989 ("OBRA 1989"))

OBRA 1989 added additional restrictions on the circumstances under which dividends paid with respect to employer securities held by an employee stock ownership plan could be deducted. The changes generally applied to employer securities acquired after August 4, 1989, but did not apply to securities acquired pursuant to a written binding contract in effect on August 4, 1989. A separate exception was provided to employer securities acquired pursuant to a tender offer registered with the Securities and Exchange Commission in effect on August 4, 1989.

If the Act had been in effect, the written binding contract exception would not have been a limited tax benefit even if it benefited 10 or fewer taxpayers, because it would have satisfied the binding contract exception. August 4, 1989, was the date of introduction of a House bill containing the provision and, therefore, the binding contract date was contemporaneous with the date of Congressional action specifying such date.

In contrast, the exception for tender offers would have been a limited tax benefit (assuming it benefitted 10 or fewer beneficiaries), because it would not have satisfied the binding contract or other legally enforceable obligation exception.

6. Various transition rules from the Tax Reform Act of 1986

The "1986 Act" contained a number of transition rules that were clearly targeted to only one taxpayer (and, in some cases, even referred to the taxpayer by name). Each of these provisions would have been limited tax benefits. The following are examples of these transition rules:

- ". . . indebtedness (which was outstanding on May 29, 1985) of a corporation incorporated on June 13, 1917, which has its principal place of business in Bartlesville, Oklahoma" (sec. 1215(c)(2)(C) and (D) of the 1986 Act).

- "In the case of an affiliated group of domestic corporations the common parent of which has its principal office in New Brunswick, New Jersey, and has a certificate of organization which was filed with the Secretary of the State of New Jersey on November 10, 1887 . . . " (sec. 1215(c)(6)(A) of the 1986 Act).

- A facility if "(i) such facility is to be used by both a National Hockey League team and a National Basketball Association team, (ii) such facility is to be constructed on a platform using air rights over land acquired by a State authority and identified as site B in a report dated May 30, 1984, prepared for a State urban development corporation, and (iii) such facility is eligible for real property tax (and power and energy) benefits pursuant to State legislation approved and effective as of July 7, 1982" (sec. 1317(3)(S) of the 1986 Act).

- "A project is described in this subparagraph if such project is consistent with an urban renewal plan adopted or ordered prepared before August 28, 1986, by the city council of the most populous city in a state which entered the Union on February 14, 1859" (sec. 1317(6)(U) of the 1986 Act).

- A facility if "(i) such facility is to be used for an annual civic festival, (ii) a referendum was held in the spring of 1985 in which voters permitted the city council to lease 130 acres of dedicated parkland to such festival, and (iii) the city council passed an inducement resolution on June 19, 1986" (sec. 1317(7)(J) of the 1986 Act).

- A residential rental property if "(i) it is a new residential development with approximately 98 dwelling units located in census tract No. 4701, and (ii) there was an inducement ordinance for such project adopted by a city council on August 14, 1984" (sec. 1317(13)(M) of the 1986 Act).

- "A facility is described in this subparagraph if it consists of the rehabilitation of the Andover Town Hall in Andover, Massachusetts" (sec. 1317(27)(I) of the 1986 Act).

- Proceeds of an issue if "(i) such issue is issued on behalf of a university established by Charter granted by King George II of England on October 31, 1754, to accomplish a refunding (including an advance refunding) of bonds issued to finance 1 or more projects, and (ii) the application or other request for the issuance of the issue to the appropriate State issuer was made by or on behalf of such university before February 26, 1986" (sec. 1317(33)(C) of the 1986 Act).

7. Technical correction to a limited tax benefit

The Tax Reform Act of 1986 included a transition rule with respect to ". . . indebtedness (which was outstanding on May 29, 1985) of a corporation incorporated on June 13, 1917, which has its principal place of business in Bartlesville, Oklahoma". As noted above, this provision would be a limited tax benefit. Suppose that, after enactment of this provision, it was discovered that the relevant date of incorporation was June 15, 1917. A provision changing the date of the incorporation would be considered a technical correction and therefore would not be a limited tax benefit (assuming the technical correction had no revenue loss), even though the original provision would have been a limited tax benefit.

APPENDICES

Appendix A.--Legislative History Cites to the Line Item Veto Act in Chronological Order

House Bill (H.R. 2)

- Report of the House Committee on Rules, House Report 104-11, Part 1 (January 27, 1995)
- Report of the House Committee on Government Reform and Oversight, House Report 104-11, Part 2 (January 30, 1995)
- Congressional Record, January 31, 1995, H970-97
- Report of the House Committee on Rules, House Report 104-15 (February 1, 1995)
- H. Res. 55, February 1, 1995
- Congressional Record, February 1, 1995, H1052-1073
- Congressional Record, February 2, 1995, H1078-1157
- Congressional Record, February 3, 1995, H1167-1198
- Congressional Record, February 6, 1995, H1208 and H1225-1264

Senate Bill (S. 4)

- Report of the Senate Committee on the Budget, Senate Report 104-9 (February 27, 1995)
- Report of the Senate Committee on Governmental Affairs, Senate Report 104-13 (March 7, 1995)
- S. 4, March 7, 1995
- Congressional Record, March 20, 1995, S4153-4187, S4187-4196, and S4203
- Congressional Record, March 21, 1995, S4210, S4212-4260, and S4293
- Congressional Record, March 22, 1995, S4301-S4358
- Congressional Record, March 23, 1995, S4409- S4486

Conference Agreement (S. 4)

- House-Senate Conference Report, House Report 104-191 (March 21, 1996)
- Congressional Record, March 21, 1996, H2640-2652
- Congressional Record, March 27, 1996, S2925, S2927, and S2929-2995
- Congressional Record. March 28, 1996, H2972-H3028
- Congressional Record, March 28, 1996, H3169
- Congressional Record, March 28, 1996, S3153

Appendix B.--Letter From Senators Dole, Domenici, and Packwood to Senators Daschle, Exon, and Glenn

United States Senate

WASHINGTON, DC 20510

March 22, 1995

The Honorable Tom Daschle
Minority Leader
United States Senate
Washington, D.C. 20510

The Honorable James Exon
Ranking Member,
Budget Committee
United States Senate
Washington, D.C. 20510

The Honorable John Glenn
Ranking Member,
Governmental Affairs Com.
United States Senate
Washington, D.C. 20510

Dear Colleagues:

Thank you for your March 21, 1995 letters to each of us concerning the substitute line-item veto measure, "The Separate Enrollment and Line-Item Veto Act of 1995," that is pending before the Senate. We welcome the opportunity to respond to your questions, which primarily relate to the bill's definition of a "targeted tax benefit."

We are concerned, however, that implicit in your questions is a fundamental misunderstanding of the objectives of the substitute. The treatment of targeted tax benefits mirrors the treatment of special interest, spending provisions in authorization or appropriation bills. Fairness dictates that if rifleshot spending provisions are subject to the veto pen, then rifleshot tax provisions benefitting a single taxpayer or a handful of taxpayers should also be subject to the veto pen. It may be too simple to suggest that we all know them when we see them -- but common sense should be an obvious test in these matters.

Your questions and our responses are set forth below.

1. *The definition of the term "targeted tax benefit" refers to any provision that loses revenue "within the periods specified in the most recently adopted concurrent resolution on the budget." Does this language mean that a provision would be considered a "targeted tax benefit" if it lost revenue in <u>any</u> year, only over the <u>entire</u> time period in the budget resolution, or in either case?*

   A provision loses revenue for purposes of the targeted tax benefit rule if the Joint Committee on Taxation estimates it loses revenue in any year covered by the most recently adopted concurrent resolution of the budget.

2. *How would provisions that raise revenue over the initial time period but then lose revenues in the out years be treated? For example, the neutral cost recovery proposal in the "Contract with America Tax Relief Act of 1995" would increase revenues over the first five years, but would lose much more ($120 billion according to the Department of the Treasury) in the out years. Assuming the Joint Committee on Taxation agrees with the estimate for the out years, would neutral cost recovery be exempt from the line-item veto because of the timing of its budget impact, despite the fact that it would dramatically increase the deficit over a 10-year period?*

If the most recently adopted concurrent resolution on the budget includes a ten-year budget period, the neutral cost recovery proposal in the "Contract With America" would be considered as losing revenue for purposes of the targeted tax benefit rule. However, as we understand it, the neutral cost recovery proposal does not favor some taxpayers over other similarly situated taxpayers and therefore would not be a targeted tax benefit.

3. *Part B of the "targeted tax benefit" definition refers to favorable treatment only "when compared with other similarly situated taxpayers." What does the phrase "similarly situated" mean? What sort of standard does it create? How would it be used to determine which provisions are subject to line-item veto authority and which are not?*

A targeted tax benefit is one that (a) loses revenue in a specified period, (b) is targeted to a single taxpayer or a limited group of taxpayers, and (c) treats the targeted taxpayers more favorably than other taxpayers in the same or similar circumstances. The concept of "similarly situated taxpayers" is an important one. A provision that only affects a few taxpayers is not in and of itself a targeted tax benefit. Because of the complex nature of our economy, there are many instances in which there are only a relatively small number of taxpayers engaged in a particular activity. If all taxpayers engaged in a particular activity are treated the same, then there is no targeted tax benefit; however, if some of those taxpayers are given more favorable tax treatment, there would be a targeted tax benefit.

For example, the current tax code has a provision that eases the estimated tax requirements on farmers based on the fact that the income of farmers is particularly difficult to estimate. Farmers' earnings are at the mercy of a host of natural events, such as weather, insects and disease. If the estimated tax rule were enacted after the line-item veto measure, it would not be a targeted tax benefit because all similarly situated taxpayers (i.e., farmers) are treated the same.

The determination of whether or not a provision is a targeted tax benefit is based on the substance of the provision, not just the form in which it is drafted. That's why the pending bill applies the targeted tax benefit concept to a provision having the practical effect of providing more favorable tax treatment.

4. *Current law includes a definition of tax expenditure that has been in place for many years. How does the definition contained in "The Separate Enrollment and Item Veto Act of 1995" relate to the existing statutory definition of tax expenditures?*

The targeted tax benefit concept in the pending bill does not change the current law definition of tax expenditures (found in section 3(3) of The Congressional Budget Act of 1974). The targeted tax benefit concept is intended to be a narrower concept than the tax expenditure concept. A targeted tax benefit gives favorable tax treatment to a single taxpayer or a limited group of taxpayers. The tax expenditure concept includes any special exclusion, exemption, or deduction from gross income, special tax credit, preferential tax rate, or deferral of tax liability. For example, the President's education deduction proposal would be a tax expenditure but would not be a targeted tax benefit.

5. *Based upon the statutory definition, both the Treasury and the Joint Committee on Taxation publish descriptions and revenue estimates of over 120 different tax expenditures. Which of the items on the current list of tax expenditures would be considered a "targeted tax benefit?" Which items would not be considered "targeted tax benefits?" Are there any other items that do not conform to the current law definition that would be included in the "targeted tax benefit" definition? If so, what are they?*

None of the items on the current tax expenditure list would be a targeted tax benefit because the pending line-item veto bill does not apply to current law provisions.

6. *Is the term "targeted tax benefit" limited to items found only in the income tax or does it also apply to excise or estate and gift tax provisions?*

The targeted tax benefit concept applies to all federal taxes.

7. *Does the definition of "targeted tax benefit" apply to provisions that would change the basic structure of the tax code? For example, would a change in the top marginal tax rate be considered a "targeted tax benefit?" How about a reduction in the statutory tax rate on capital gains?*

The targeted tax benefit concept does not apply to changes in the basic structure of the tax code. For example, an across-the-board tax cut on wage and salary income of all individuals would not be a targeted tax benefit. Likewise, an across-the-board tax cut on capital gains of all individuals would not be a targeted tax benefit.

8. *The language of "The Separate Enrollment and Item Veto Act of 1995" refers to "new" direct spending and "new" targeted tax benefits. In this case, the word "new" seems open to a number of interpretations that need clarification. Does the lowering of an existing tax rate constitute a "new" tax benefit or is it merely a modification of an existing tax benefit and therefore not subject to the line-item veto? Would an increase in the health insurance deduction for the self-employed be considered "new," or would it be exempt from the item-veto?*

The term "new" refers to a provision that creates a new program or modifies an existing program and increases direct spending. In the context of a targeted tax benefit, the term "new" means any targeted tax benefit enacted after the effective date of the pending legislation. Because the health insurance deduction treats similarly situated taxpayers (i.e., self-employed individuals) the same, a future increase in the health insurance deduction would not be a targeted tax benefit.

9. *The language on "targeted tax benefits" clearly refers only to provisions that lose revenue and thereby increase the deficit. No similar restriction appears for direct spending programs. Would the bill thus subject any entitlement change (including those that actually produce savings) to the line item-veto?*

No, the pending line-item veto bill applies only to entitlement changes which increase direct spending.

10. *On the entitlement side, how would provisions that repeal an existing program and replace it with a different program be treated? Would each part of the proposal be subject to the veto pen separately? That is, could the President veto the repeal of the existing program but leave in place the new and different program?*

The pending line-item veto bill applies separately to each new direct spending provision. Presumably repeal of an existing entitlement program would result in a reduction in spending (rather than an increase in direct spending) and therefore the President would not be able to line-item veto that provision.

11. *Finally, would the veto authority provided in the amendment extend to Reconciliation measures? The current Byrd Rule formulation appears to protect Reconciliation titles that meet the Budget Committee savings instruction, even if the titles contain the deficit increasing measures. Would this bill change that approach?*

The pending line-item bill applies to reconciliation bills only if the reconciliation bill includes new direct spending or new targeted tax benefit provisions. The line-item veto bill is independent of the Budget Act and does not change the application of section 313 of the Budget Act (the Byrd Rule) to reconciliation bills. Compliance with the Byrd Rule (section 313 of the Budget Act) or the budget resolution's reconciliation instructions do not protect a reconciliation bill from separate enrollment. Just as appropriations bills are subject to the line-item veto procedures even if they comply with the Budget Act's statutory caps and the budget resolution's budget allocations, reconciliation bills are subject to the line-item veto procedures even if they comply with the budget resolution's reconciliation directives and the Byrd Rule.

We hope our responses to your questions are helpful to you. If you need further information, please do not hesitate to contact us.

Sincerely,

BOB DOLE

PETE DOMENICI

BOB PACKWOOD